



Brussels, 15.9.2016
SWD(2016) 312 final

COMMISSION STAFF WORKING DOCUMENT

Preliminary Report on the E-commerce Sector Inquiry

COMMISSION STAFF WORKING DOCUMENT

Preliminary Report on the E-commerce Sector Inquiry

Table of Contents

EXECUTIVE SUMMARY	8
A. INTRODUCTION	12
1. THE WIDER CONTEXT: THE DIGITAL SINGLE MARKET STRATEGY	12
2. THE REASONS FOR LAUNCHING THE SECTOR INQUIRY	13
3. THE PURPOSE OF THE SECTOR INQUIRY	19
4. ANALYTICAL FRAMEWORK	20
5. SELECTION OF ADDRESSEES: GOODS	24
5.1 Selection of retailers	24
5.2 Selection of manufacturers	25
5.3 Selection of marketplaces, price comparison tools and payment system providers	25
5.4 Responses received	25
6. SELECTION OF ADDRESSEES: DIGITAL CONTENT	27
6.1 Selection of digital content providers (retail markets)	27
6.2 Selection of right holders (wholesale markets)	29
B. E-COMMERCE IN GOODS	31
1. CHARACTERISTICS OF RESPONDENTS	31
1.1 Retailers	31
1.2 Manufacturers	34
1.3 Marketplaces	36
1.4 Price comparison tools	40
1.5 Payment service providers	44
2. MAIN FEATURES OF COMPETITION IN E-COMMERCE IN GOODS	45
2.1 The concentration of manufacturers and retailers in the sectors covered by the sector inquiry	45
2.2 Main parameters of competition	46
2.3 Pricing	53
2.4 Differences between online and offline offers	56
2.5 The manufacturers' reaction to the growth of e-commerce	57
3. DISTRIBUTION	61
3.1 Online and offline distribution strategies	62
3.1.1 Retailers' distribution strategies	62
3.1.2 Manufacturers' distribution strategies	62
3.2 Developments with regard to distribution strategies	63
3.3 Distribution by manufacturers	66
3.4 Distribution via independent retailers	69
3.4.1 Introduction	69
3.4.2 Territorial exclusive distribution agreements	69
3.4.2.1 Prevalence of territorial exclusive distribution	70

3.4.2.2	Reasons for using territorial exclusive distribution agreements.....	73
3.4.3	Selective distribution.....	76
3.4.3.1	Overview and development of selective distribution.....	76
3.4.3.2	The reasons for opting for selective distribution.....	80
3.4.3.3	The selection criteria.....	82
3.4.3.4	Pure online players in selective distribution.....	87
3.4.3.5	General considerations on selective distribution.....	88
3.4.4	Agency agreements.....	90
4.	RESTRICTIONS TO SELL AND ADVERTISE ONLINE.....	92
4.1	Motivations for restrictions.....	92
4.1.1	Product quality, brand image and price.....	93
4.1.2	Customer services, promotion and advertising.....	93
4.1.2.1	Types of customer services.....	94
4.1.2.2	Financing of customer services.....	96
4.1.2.3	Promotion and advertising.....	98
4.1.3	Customers' purchasing behaviour and free-riding between the online and offline retail channel.....	101
4.2	Overview of restrictions.....	106
4.3	Cross-border e-commerce and geographic restrictions to sell and advertise online.....	109
4.3.1	Geographic sales strategies of manufacturers.....	110
4.3.2	Geographic sales strategies of retailers and cross-border e-commerce.....	112
4.3.2.1	Retailers not selling cross-border.....	112
4.3.2.2	Cross-border visits and transactions on retailers' own websites.....	115
4.3.2.3	The role of online marketplaces for cross-border sales....	117
4.3.2.4	The role of price comparison tools for cross-border sales	119
4.3.2.5	Geo-blocking measures.....	120
4.3.2.6	Geo-filtering and cross-border price and offer differences	122
4.3.2.7	Commercial reasons for not selling cross-border and costs of supplying abroad.....	125
4.3.3	Contractual territorial restrictions to sell and advertise online	127
4.3.3.1	Agreements between manufacturers and retailers restricting cross-border online sales.....	127
4.3.3.2	Monitoring of customer location.....	131
4.3.3.3	Geo-blocking measures, territorial restrictions and the EU competition rules.....	131
4.3.3.4	Indications of contractual territorial restrictions.....	135
4.4	Restrictions to sell on online marketplaces.....	136
4.4.1	Importance of marketplaces as a sales channel for retailers ..	137

4.4.2 Impact of sales through marketplaces on the business of manufacturers	143
4.4.3 Prevalence and characteristics of marketplace restrictions	144
4.4.4 Reasons put forward for marketplace restrictions by manufacturers	148
4.4.5 Reasons for marketplace restrictions reported mainly by retailers and some marketplaces	150
4.4.6 Possibilities offered by marketplaces to address quality requirements	151
4.4.7. Notice and take down procedures on marketplaces	151
4.4.8 Marketplace restrictions under EU competition rules	152
4.5 The use of price comparison tools and restrictions on the use of price comparison tools	157
4.5.1 Usage of price comparison tools by retailers	157
4.5.2 Restrictions on the use of price comparison tools	160
4.5.3 Reasons put forward for restrictions to use price comparison tools	163
4.5.4 Restrictions on the use of price comparison tools under EU competition rules	165
4.6 Pricing restrictions	167
4.6.1 Price setting at retail level	167
4.6.2 Monitoring of recommended retail prices	170
4.6.3 Retailers' compliance with price indications and reasons	172
4.6.4 Charging different wholesale prices for different sales channels	173
4.6.5 Online price transparency and the use of price monitoring software	174
4.7 Exclusivity and parity agreements between retailers and marketplaces and/or price comparison tools	176
4.7.1 Agreements between retailers and marketplaces	177
4.7.2 Agreements between retailers and price comparison tools	179
4.8 Other types of restrictions to sell or advertise online	179
5. OTHER OBSERVATIONS	182
5.1 Customer data	182
C. E-COMMERCE IN DIGITAL CONTENT	186
1. CHARACTERISTICS OF RESPONDENTS	186
1.1 Digital content providers	186
1.1.1 Types of operators	186
1.1.2 Business models	187
1.1.3 Size of activities	189
1.1.4 Revenue breakdown and advertising revenues	190
1.2 Right holders	192
1.2.1 Types of right holders	192

1.2.2 Size of activities of right holders.....	192
1.3 Types of content	193
2. MARKET TRENDS AND LICENSING PRACTICES	195
2.1 Market trends in the provision of online digital content services.....	195
2.2. Licensing practices	195
3. THE SCOPE OF LICENSED RIGHTS: TECHNOLOGIES.....	196
3.1 Definitions and data set	196
3.2. The scope of reception technology rights	207
3.3 The scope of ancillary and usage rights	210
3.4 Exclusive technology rights	214
3.5 Bundling of rights.....	216
3.5.1 Prevalence of bundling of rights	216
3.5.2 Bundling of rights.....	218
4. THE SCOPE OF LICENSED RIGHTS: TERRITORIES	219
4.1 Introduction	219
4.2 The territorial scope of online rights	219
4.2.1 The territorial scope of online rights in relation to different types of digital content	221
4.2.2 The territorial scope of online rights in relation to different types of digital content providers	222
4.2.3 The territorial scope of online rights in relation to the different business models used by digital content providers.....	224
4.3 Exclusive territorial rights	225
4.4 Reasons for non-availability of content across borders	226
4.5 Catalogue differences	229
4.6 Reasons for catalogue differences	230
4.7 Reasons provided by right holders why online rights are not licensed for certain territories.....	231
4.8 Geo-blocking of digital content services.....	232
4.8.1 Existence and extent of geo-blocking	232
4.8.2 Geo-blocking required by licensing agreements	236
4.8.3 Geo-blocking measures used to restrict cross border access and portability.....	238
4.8.4 Restrictions on access and use in the terms of service for users.....	240
4.8.4.1 Unilateral restrictions on access and use in the terms of service for users.....	240
4.8.4.2 Contractual restrictions on access and use in the terms of service for users.....	241
4.9 Contractual provisions concerning monitoring, sanctions and compensation in relation to geo-blocking	243
4.9.1 Monitoring provisions	244

4.9.2 Sanctions and compensation for non-compliance with territorial and geo-blocking clauses	247
4.10 Use of VPN and IP routing services	250
5. THE SCOPE OF LICENSED RIGHTS: RELEASE WINDOWS	251
6 EXCLUSIVE RIGHTS IN CONTENT IN THE LICENSING AGREEMENTS BETWEEN RIGHT HOLDERS AND DIGITAL CONTENT PROVIDERS	254
7. DURATION OF LICENSING AGREEMENTS AND CONTRACTUAL RELATIONSHIPS	259
7.1 Duration of on-going licensing agreements	260
7.2 First time agreements	261
7.3 Length of the existing contractual relationships.....	262
7.4 Renewal clauses and rights of first refusal.....	264
7.4.1 Right of first refusal	264
7.4.2 Renewal clauses	266
7.5 Matching offer rights.....	267
8. PAYMENT STRUCTURES IN DIGITAL CONTENT LICENSING AGREEMENTS	268
8.1 Definitions and data set	268
8.2 Payment structures for online rights: Overall, by product type and by type of operator	270
8.3 Payment structures: combinations of specific payment mechanisms	276
8.4 Level of Payments	277
9. FINANCING OF DIGITAL CONTENT PRODUCTS	279
D. KEY PRELIMINARY FINDINGS	282
1. KEY PRELIMINARY FINDINGS: GOODS	282
1.1 Key features of e-commerce with a substantial effect on distribution strategies.....	282
1.1.1 Price transparency leading to an increase in price competition.....	282
1.1.2 Free-riding	282
1.1.3 Increased direct retail activities by manufacturers	282
1.1.4 Expansion of selective distribution	282
1.2 Potential barriers to competition	283
1.2.1 Cross-border sales restrictions.....	283
1.2.2 Restrictions on the use of marketplaces	283
1.2.3 Restrictions on the use of price comparison tools.....	284
1.2.4 Pricing restrictions.....	284
2. KEY PRELIMINARY FINDINGS: DIGITAL CONTENT.....	285
2.1 Licensing of rights: A key factor for competition in online digital content services	285
2.2 Contractual restrictions in relation to transmission technologies, timing of releases and territories.....	286
2.3 Duration of the agreements	287
2.4 Payment structures.....	287

2.5 Impact of licensing practices	288
E. LAUNCH OF THE PUBLIC CONSULTATION.....	290

EXECUTIVE SUMMARY

Introduction

On 6 May 2015, the European Commission ("Commission") decided on the basis of European Union ("EU") competition rules to launch a sector inquiry into the electronic commerce ("e-commerce") of consumer goods ("goods") and digital content in the EU ("sector inquiry") as part of its Digital Single Market strategy adopted on the same day. Promoting e-commerce is a key part of this strategy. The e-commerce sector inquiry aims at obtaining an overview of the prevailing market trends, gathering evidence on potential barriers to competition linked to the growth of e-commerce and understanding the prevalence of certain, potentially restrictive, business practices and the underlying rationale for their use.

E-commerce in the EU has grown steadily over the past years. Today the EU is the largest e-commerce market in the world. The percentage of individuals aged 16 to 74 having ordered goods or services over the internet, has continuously grown from 30 % in 2007 to 53 % in 2015.

E-commerce in goods

In the course of the sector inquiry the Commission has received information from a large number of market players, including retailers, manufacturers, marketplaces, price comparison tools and online payment service providers, active in the following product categories: clothing and shoes, consumer electronics, electrical household appliances, computer games and software, toys and childcare articles, media (books, CDs, DVDs and Blu-ray discs), cosmetics and healthcare products, sports and outdoor equipment as well as house and garden.

The preliminary results of the sector inquiry show that online and offline competition may take place on several parameters such as price, product quality, brand image, novelty and time of release. With regard to e-commerce, the increased online price transparency is the feature that most affects the behaviour of market players and customers.

First, price transparency directly affects customer behaviour. It lowers search costs for customers who are able to instantaneously obtain and compare product and price information online, and switch swiftly from one channel (online/offline) to another. This allows customers to find the best deal online but may also result in *free-riding* across sales channels. For instance, customers may use pre-sale services of brick and mortar shops but purchase the product online or, the other way round, search and compare products online before purchasing in brick and mortar shops. Finding a lawful solution to address free-riding and maintaining the incentives of retailers to invest in high quality services by creating a level-playing field between offline and online sales channels, given the cost structures, is a key consideration for both manufacturers and retailers.

Second, the ability to directly compare prices of products across a number of online retailers, leads to increased price competition, affecting both online and offline sales. Such increased price competition has immediate beneficial effects for customers. It may however have drawbacks for competition on other parameters than price, such as quality, brand and

innovation. Price is considered as the key parameter of competition among retailers, while quality and brand image considerations are pointed out by manufacturers as the most important features of competition between brands (inter-brand competition). Keeping control over the image and positioning of their brand is a key concern for many manufacturers in the mid- to long term.

Third, online price transparency not only helps customers to secure the cheapest deal, it also allows companies to easily monitor each other's prices. The majority of retailers track online prices, and more than two thirds do it via automatized software programmes developed for that purpose. Nearly 80 % of those retailers that use software to track prices consequently adjust their own prices to those of their competitors. Manufacturers also have increased possibilities to monitor deviations from "recommended" retail prices.

The emergence of alternative online distribution models, such as online marketplaces, facilitates access to customers. Smaller retailers may, with limited investment efforts, become visible and sell products to a large customer base and in multiple Member States through marketplaces.

The preliminary results show that sales via marketplaces generate a high share of the online revenues of smaller retailers which use both own websites as well as marketplaces for selling goods online, but that an own online shop remains important for most retailers. There are significant differences across Member States in the proportion of retailers who use marketplaces: 62 % of retailers in Germany reported that they were selling via marketplaces, 43 % of the retailers from the United Kingdom, and 36 % of the retailers in Poland, while the proportion in other Member States is lower than one third of the retailers. The importance of marketplaces also varies between product categories, with marketplaces being most relevant for retailers selling clothing and shoes or consumer electronics.

The above market trends affect distribution and pricing strategies of manufacturers and retailers significantly.

First, as a reaction to increased online price transparency and price competition, manufacturers seek a "tighter" control over distribution with a view to better controlling price and quality of distribution. The preliminary results of the sector inquiry show an increased tendency for manufacturers to engage in retailing: 64 % of the manufacturers report that they opened own online retail shops in the last 10 years as a reaction to the growth of e-commerce, thereby on the one hand benefitting from a direct sales channel to customers while, on the other hand, keeping full control of retail quality and price.

A second trend is the increased recourse to selective distribution systems. While the majority of distribution takes place in open distribution systems, the sector inquiry shows an increase, over the past decade, in the use of selective distribution where manufacturers can set the quality criteria that retailers need to meet in order to become part of the distribution network and where all sales to unauthorized retailers are prohibited. Manufacturers explicitly acknowledge that they use selective distribution as a reaction to the growth of e-commerce, allowing them a better control of distribution quality and, indirectly, price. 56 % of the

respondent manufacturers report that they make use of selective distribution for at least part of their products. Nearly 20 % of the respondent manufacturers introduced selective distribution systems in the last decade (where they did not have one before), as a reaction to the growth of e-commerce, and two thirds of the respondent manufacturers that already used selective distribution introduced new criteria in their distribution agreements in relation to how retailers should sell or advertise their products online.

Third, manufacturers also react to the growth of e-commerce by increasingly using vertical restraints to keep better control over the distribution of their products. Depending on their business models and priorities, vertical restraints may take various forms, such as pricing restrictions, and restrictions to sell or advertise through certain online channels or to sell cross-border. For example, distribution agreements containing marketplace restrictions were reported by 18 % of the retailers.

The preliminary results also show that 36 % of retailers do not sell cross-border for at least one of the product categories they are selling. Retailers use geo-blocking measures to restrict cross-border sales. 38 % of retailers collect data on the location of their customers, with a view to applying geo-blocking measures. However, the majority of those geo-blocking measures are based on unilateral business decisions of retailers. Geo-blocking most commonly takes the form of refusal to deliver to customers in other Member States, followed by refusals to accept payments from such customers. Nearly 12 % of retailers indicate that they have contractual cross-border sales restrictions in at least one product category that they are selling.

Manufacturers also report about the growing market shares and thus strong negotiating positions of certain large retailers, exercising increased pressure on manufacturers to, either contractually or de facto, and either regularly or on a more ad hoc basis, guarantee their profit margins, compensate for losses/ lower profits than expected, or otherwise ensure that a certain minimum price is applied throughout the distribution network.

As a follow-up to the sector inquiry, the Commission may investigate further the compatibility with the EU competition rules of certain practices, such as pricing restrictions, restrictions on online sales and territorial restrictions.

E-commerce in digital content

One of the key determinants of competition in digital content markets is the availability of licences from the holders of the copyrights in the content. The availability of rights for online transmission is largely determined by the scope of rights as defined in the licensing agreements. Licensing agreements between sellers of rights, i.e. right holders, and buyers of rights, i.e. digital content providers use complex definitions to precisely define the scope of rights. Different rights are distinguished in licensing agreements, in particular in terms of technological, temporal and territorial scope. Contractual restrictions with respect to the licensed rights are widespread and indeed the norm.

Exclusivity is widely used in relation to the licensed rights since access to exclusive content increases the attractiveness of the offer of digital content providers.

About 70 % of respondent digital content providers restrict access to their digital content for users from other Member States. However there are relatively large differences in the extent to which geo-blocking is used both between different types of business models and between Member States. Geo-blocking mostly results from contractual restrictions in agreements between digital content providers and right holders. Almost 60 % of respondent digital content providers are contractually required by right holders to geo-block. Geo-blocking is most prevalent in agreements for films, sports and TV series. Licensing agreements enable right holders to monitor content providers' use of geo-blocking measures or compliance with territorial restrictions and to impose sanctions and ask for compensation if such measures or territorial restrictions are not complied with.

A substantial number of licensing agreements are concluded for rather long durations or include clauses that facilitate prolongation of the agreements.

The preliminary results of the sector inquiry raise the question whether some of the current licensing practices may make it more difficult for new online business models and services to emerge and for new or smaller players to enter the market or expand their activities into other markets, in particular cross-border due to geo-blocking requirements. This may be particularly true when online rights are sold exclusively on a per Member State basis or bundled with rights in other transmission technologies and then remain unused.

The Commission will therefore assess on a case-by-case basis, having regard to the characteristics of the specific product and geographic markets, whether certain licensing practices restrict competition and whether enforcement of the EU competition rules by the Commission is necessary in order to ensure effective competition.

Launch of the public consultation

This Preliminary Report provides an overview of the main competition-relevant market trends identified in the sector inquiry in relation to e-commerce and identifies possible competition concerns. With the publication of this Preliminary Report, the Commission wishes to trigger a facts-based exchange of views with stakeholders.

For this purpose, DG Competition is soliciting the views and comments of interested stakeholders about the preliminary findings of the sector inquiry presented in this Preliminary Report. All stakeholders are invited to submit their comments on this report not later than 18 November 2016. All comments should be sent to the following e-mail address: COMP-E-COMMERCE@ec.europa.eu.

The Final Report of the sector inquiry is expected to be published in the first quarter of 2017.

A. INTRODUCTION

1. THE WIDER CONTEXT: THE DIGITAL SINGLE MARKET STRATEGY

- (1) On 6 May 2015, the Commission adopted the Digital Single Market strategy.¹
- (2) The Digital Single Market strategy outlines several key actions under three pillars by means of which the Commission envisages to create a Digital Single Market. One of these pillars relates to ensuring better access for consumers and businesses to goods and services via e-commerce across the EU.
- (3) Under this pillar the Commission has already undertaken and will shortly undertake several actions, including legislative proposals in the following areas: (i) harmonised EU rules on contracts for the supply of digital content and for the online and other distance sales of goods² and the cooperation between national authorities responsible for the enforcement of consumer protection laws,³ (ii) efficient and affordable cross-border parcel delivery,⁴ (iii) unjustified geo-blocking,⁵ (iv) simplified VAT regimes,⁶ and (v) copyright modernisation.⁷ The Commission also undertook to assess the role of online platforms and intermediaries.⁸
- (4) Under this pillar of the Digital Single Market strategy, the Commission decided on 6 May 2015, on the basis of the EU competition rules, pursuant to Article 17 of

¹ Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions "A Digital Single Market Strategy for Europe", COM(2015) 192 final.

² Proposal for a directive of the European Parliament and of the Council on certain aspects concerning contracts for the supply of digital content, COM(2015) 634 final; and Proposal for a directive of the European Parliament and of the Council on certain aspects concerning contracts for the online and other distance sales of goods, COM(2015) 635 final.

³ Proposal for a Regulation of the European Parliament and of the Council on cooperation between national authorities responsible for the enforcement of consumer protection laws, COM(2016) 283 final.

⁴ Proposal for a Regulation of the European Parliament and of the Council on cross-border parcel delivery services, COM(2016) 286 final.

⁵ Proposal for a Regulation of the European Parliament and of the Council on addressing geo-blocking and other forms of discrimination based on customers' nationality, place of residence or place of establishment within the internal market and amending Regulation (EC) No 2006/2004 and Directive 2009/22/EC, COM(2016) 289 final.

⁶ Communication from the Commission to the European Parliament, the Council and the European Economic and Social Committee on an action plan on VAT, COM(2016) 148 final; and Inception impact assessment on "Modernising VAT for cross-border e-commerce", Available at the following address: http://ec.europa.eu/smart-regulation/roadmaps/docs/2016_taxud_002_iaa_vat_en.pdf.

⁷ Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: Towards a modern, more European copyright framework COM(2015) 626 final; and Proposal for a Regulation of the European Parliament and of the Council on ensuring the cross-border portability of online content services in the internal market, COM(2015) 627 final.

⁸ Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions: Online Platforms and the Digital Single Market, Opportunities and Challenges for Europe, COM(2016) 288 final.

Regulation 1/2003,⁹ to launch a sector inquiry into trade of goods and digital content in e-commerce in the EU.¹⁰

- (5) While most of the actions of the Digital Single Market strategy essentially seek to address regulatory barriers to cross-border online trade in goods and services, the sector inquiry investigates barriers created by companies.¹¹ The inquiry focuses on distribution agreements for goods and services that may create barriers to e-commerce. With respect to online platforms, the sector inquiry focuses on gathering information on conduct of companies active in e-commerce (notably marketplaces and price comparison tools). It does not relate to conduct of online platforms more generally. The sector inquiry therefore complements the Commission's legislative proposals and the initiatives on online platforms under the Digital Single Market strategy.

2. THE REASONS FOR LAUNCHING THE SECTOR INQUIRY

- (6) E-commerce in the EU has grown steadily over the past years. Today the EU is the largest e-commerce market in the world. The percentage of individuals aged between 16 and 74 having ordered goods or services over the internet, has continuously grown from 30 % in 2007 to 53 % in 2015.¹² The proportion of online buyers varies from Member State to Member State. The highest percentage of online buyers can be found in the United Kingdom (where 81 % of the total population aged between 16 and 74 made purchases online) and the lowest in Romania (where 11 % of the total population aged between 16 and 74 made purchases online).¹³ There is a positive correlation between the percentage of customers engaging in online shopping and the internet penetration rate.¹⁴

⁹ Council Regulation (EC) No 1/2003 of 16 December 2002 on the implementation of the rules on competition laid down in Articles 81 and 82 of the Treaty, OJ L 1, 4.1.2003, p. 1. ("Regulation 1/2003").

¹⁰ Commission decision of 6 May 2015 initiating an inquiry into the e-commerce sector pursuant to Article 17 of Council Regulation (EC) No 1/2003 (HT.4607), C(2015) 3026, final.

¹¹ For example, the Commission proposal for a Regulation of the European Parliament and of the Council on addressing geo-blocking and other forms of discrimination based on customers' nationality, place of residence or place of establishment within the internal market and amending Regulation (EC) No 2006/2004 and Directive 2009/22/EC, COM(2016) 289 final, seeks to address company-erected barriers also in the form of unilateral business decisions of non-dominant undertakings or intra-group decisions which are generally not caught by EU competition rules.

¹² See 2015 Eurostat data, available at the following address:

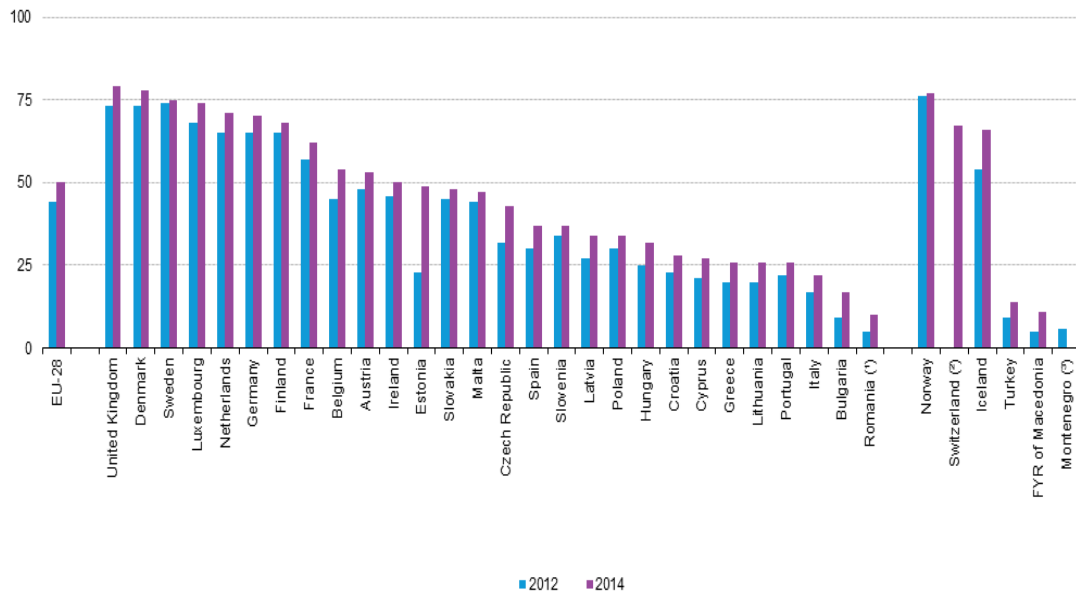
<http://ec.europa.eu/Eurostat/documents/2995521/7103356/4-11122015-AP-EN.pdf/276b6a7c-69a6-45ce-b6bf-488e975a8f5d>

See also data from Flash Eurobarometer 397 (2015), Consumers attitude towards cross-border trade and consumer protection.

¹³ Eurostat Community Survey on ICT usage in households and by individuals, 2015 (isoc_ec_ibuy).

¹⁴ Flash Eurobarometer 397 (2015). The survey was carried out between 14 and 16 April 2014. The data refer to purchases in the last 12 months.

Figure A. 1: Individuals who ordered goods or services over the internet for private use in the 12 months prior to the survey, 2012 and 2014 (%)



(*) Break in series.

(*) 2012: not available.

(*) 2014: not available.

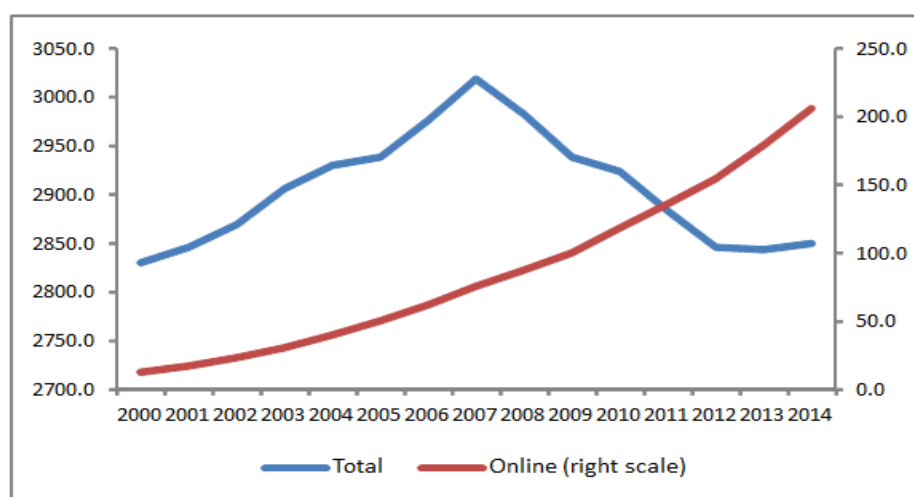
Source: Eurostat (online data code: isoc_ec_ibuy)

Source: Eurostat, 2015 Community survey on ICT usage in households and by individuals

- (7) Figure A. 2 below presents the estimated evolution of online and total retail sales in the EU between 2000 and 2014. During that period, the estimated average annual growth rate in the online sales of goods was approximately 22 %, despite the 2008 economic crisis and the drop in overall retail sales between 2007 and 2012. At the same time the proportion of companies engaging in online sales did not grow significantly between 2004 and 2014.¹⁵

¹⁵ "The European Digital Single Market: its Role in Economic Activity in the EU", Joint Research Centre of the European Commission, Institute for Prospective Technological Studies, Digital Economy Working Paper 2015/17, JRC 98723. Available at the following address: <https://ec.europa.eu/jrc/sites/default/files/JRC98723.pdf>

Figure A. 2: Estimated evolution of the total and online retail sales in goods, 2000-2014 (in billion EUR)



Source: Duch-Brown and Martens¹⁶

- (8) E-commerce in the EU is geographically concentrated: the United Kingdom, Germany and France concentrate 65 % of EU online sales.¹⁷
- (9) The proportion of individuals aged between 16 and 74 in the EU, who ordered goods or services over the internet for private use reached 50 % in 2014.¹⁸ Despite the growth of e-commerce, in the same year only 15 % shopped online from a seller established in another Member State.¹⁹

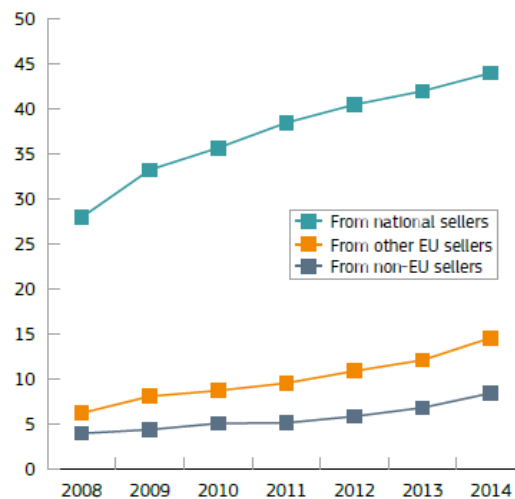
¹⁶ Nestor Duch-Brown and Bertin Martens: "The European Digital Single Market: its Role in Economic Activity in the EU", Joint Research Centre of the European Commission, Institute for Prospective Technological Studies, Digital Economy Working Paper 2015/17, JRC 98723. Available at the following address: <https://ec.europa.eu/jrc/sites/default/files/JRC98723.pdf>

¹⁷ Nestor Duch-Brown and Bertin Martens: "The European Digital Single Market: its Role in Economic Activity in the EU", Joint Research Centre of the European Commission, Institute for Prospective Technological Studies, Digital Economy Working Paper 2015/17, JRC 98723. Available at the following address: <https://ec.europa.eu/jrc/sites/default/files/JRC98723.pdf>

¹⁸ Eurostat, Digital Single Market: promoting e-commerce for individuals. Available at the following address: http://ec.europa.eu/Eurostat/data/database?node_code=isoc_bdek_smi

¹⁹ Eurostat Community Survey on ICT usage in households and by individuals 2014 (isoc_ec_ibuy). See also Consumer Conditions Scoreboard 2015. Available at the following address: http://ec.europa.eu/consumers/consumer_evidence/consumer_scoreboards/11_edition/docs/ccs2015scoreboard_en.pdf

Figure A. 3: Domestic and cross-border online shopping, EU-28, 2008-2014 (%)



Source: Eurostat²⁰

- (10) Similarly, Eurostat data reveal that in 2014 in the EU 19 % of companies engaged in online sales, but only 8 % of them made online sales to customers located in other Member States. According to Eurostat, in 2014, 85.4 % of online sales of companies stem from domestic sales and 10.3 % stem from EU cross-border sales.²¹ A large mystery shopping survey conducted on behalf of the Commission at the end of 2015 found that only 37 % of websites allow cross-border EU customers to reach the stage of successfully entering payment card details, i.e. the final step before completing a purchase.²²
- (11) There are also significant differences between Member States when it comes to the proportion of customers in a particular Member State that shop online from retailers located cross-border. For example, while more than 68 % of residents of Luxembourg

²⁰ Eurostat Community Survey on ICT usage in households and by individuals 2014 (isoc_ec_ibuy). See also Consumer Conditions Scoreboard 2015. Available at the following address: http://ec.europa.eu/consumers/consumer_evidence/consumer_scoreboards/11_edition/docs/ccs2015scoreboard_en.pdf

²¹ Flash Eurobarometer 413 (2015), Companies engaged in online activities. Available at the following address: http://ec.europa.eu/public_opinion/flash/fl_413_en.pdf

See also Flash Eurobarometer 359 (2012), Retailers attitude towards cross-border sales and consumer protection according to which one quarter (25 %) of the interviewed retailers sell to consumers in at least one other EU Member State.

A comparison across Member States and some third countries shows that retailers in Belgium (45 %), Luxembourg (42 %), Slovenia (41 %) and Greece (40 %) are the most likely to sell to consumers in at least on other EU Member State. Available at the following address:

http://ec.europa.eu/consumers/consumer_evidence/market_studies/docs/geoblocking-exec-summary_en.pdf

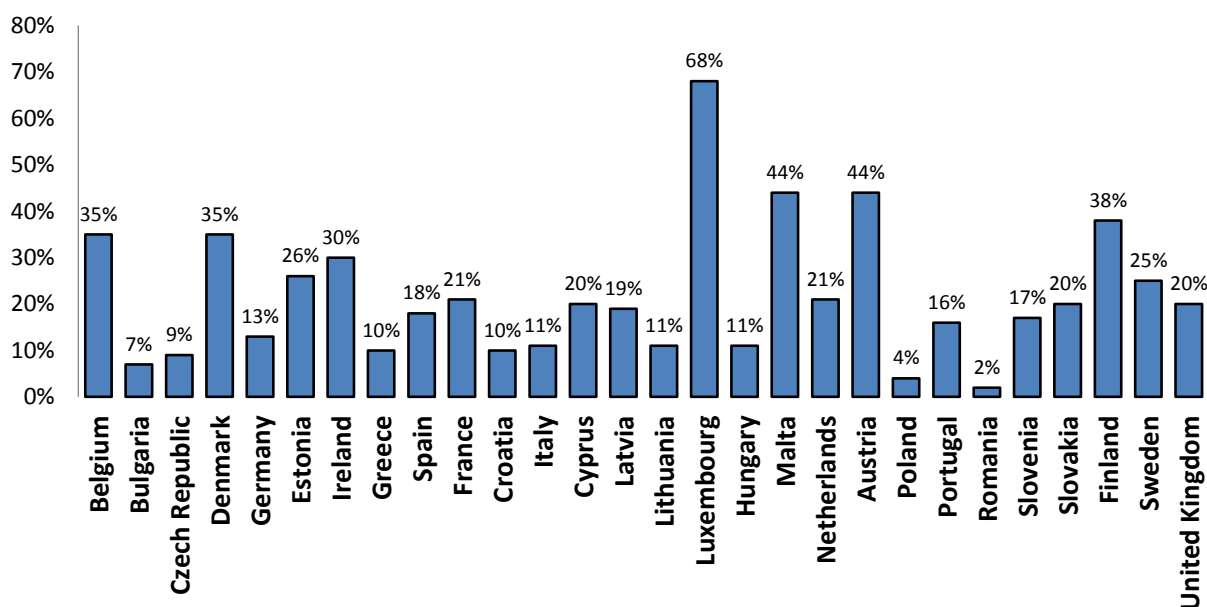
²² Mystery shopping survey on territorial restrictions and geo-blocking in the European digital single market, 2016. Available at the following address:

http://ec.europa.eu/consumers/consumer_evidence/market_studies/docs/geoblocking_final_report_2016_en.pdf

See also Melisande Cardona and Bertin Martens: Supply-side Barriers to Cross-border e-Commerce in the EU Digital Single Market, Joint Research Centre of the European Commission, Institute for Prospective Technological Studies, Digital Economy Working Paper 2014, JRC 92294. Available at the following address: https://ec.europa.eu/jrc/sites/default/files/JRC92294_Supply%20side%20barriers%20to%20ecommerce.pdf?search

engage in cross-border online shopping, only 2 % of residents of Romania do the same. As a general trend, the relative (population-weighted) intensity of cross-border e-commerce is inversely related to population size: customers in smaller Member States are more active in cross-border purchases than those of larger ones.²³

Figure A. 4: Cross-border internet purchases by individuals (percentage of total individuals) – 2015



Source: Eurostat²⁴

- (12) Digital content is one of the biggest e-commerce sectors in the EU, accounting for 33 % of online trade by individuals.²⁵ A total of 38 % of individuals participating in the Eurostat study reported using the internet to access media content online in 2014, up from 21 % in 2007, while 33 % reported buying such content online.²⁶
- (13) A Eurobarometer report²⁷ indicates that in 2014, around half of the EU citizens responding to the survey accessed or downloaded audio-visual content and music

²³ Nestor Duch-Brown and Bertin Martens: "The European Digital Single Market: its Role in Economic Activity in the EU", Joint Research Centre of the European Commission, Institute for Prospective Technological Studies, Digital Economy Working Paper 2015/17, JRC 98723. Available at the following address: <https://ec.europa.eu/jrc/sites/default/files/JRC98723.pdf>

²⁴ Eurostat, Digital Single Market: promoting e-commerce for individuals. See above.

²⁵ European Commission, Digital Agenda Scoreboard. The figure refers to the percentage of all individuals buying online who purchased digital content in 2014 in the EU-27. The data includes online games. Available at the following address:

[https://digital-agenda-data.eu/charts/see-the-evolution-of-an-indicator-and-compare-countries#chart={%22indicator-group%22:%22any%22,%22indicator%22:%22i_bgood%22,%22breakdown%22:%22IND_TOTAL%22,%22unit-measure%22:%22PC_IND_BLT12%22,%22ref-area%22:\[%22EU27%22\]}](https://digital-agenda-data.eu/charts/see-the-evolution-of-an-indicator-and-compare-countries#chart={%22indicator-group%22:%22any%22,%22indicator%22:%22i_bgood%22,%22breakdown%22:%22IND_TOTAL%22,%22unit-measure%22:%22PC_IND_BLT12%22,%22ref-area%22:[%22EU27%22]})

²⁶ Eurostat data on internet usage in the EU-28 (includes online games). Available at the following address:

http://ec.europa.eu/eurostat/estat-navtree-portlet-prod/NodeInfoServices?lang=en&code=isoc_pibi_ioa

²⁷ Flash Eurobarometer 411 (2015), Cross-border access to online content. Available at the following address:

online, with 30 % of them doing so via subscriptions or individual transactions. However only a third of them could find the audio-visual content they wanted. While a minority of customers reported trying to access online digital content cross-border (8 %), this proportion is substantially higher for younger people (17 %) and is growing, as they look for digital content which is available outside their Member State of residence. According to the same report, more than 50 % of customers have experienced problems when trying to access digital content cross-border.

- (14) Different studies point to a wide range of reasons, both on the side of customers and on the side of the retailers that may explain the modest growth of cross-border e-commerce in the EU. For instance, according to a recent Eurobarometer report, the most common difficulties companies encounter when selling online are related to cost. Retailers are concerned that delivery costs are too high (51 %), that guarantees and returns are too expensive (42 %), or that dispute resolution is too expensive (41 %).²⁸ According to the same report, for almost one third (32 %) of retailers slow internet speeds are a problem, and for 15 % of retailers, the complications or costs of dealing with foreign taxation is a major problem. Additional reasons for not engaging in cross-border sales are lack of knowledge of applicable laws and lack of foreign language skills.
- (15) When it comes to customers, they are more confident in making domestic online purchases (61 %) than they are in purchasing online from retailers in other Member States (38 %).²⁹ Surveys and studies invoke different reasons for this difference. Concerns regarding delivery and return possibilities, as well as doubts about misuse of payment card information and personal data may deter customers from shopping online from retailers in another Member State.³⁰ This adds to the more subjective obstacles to cross-border sales, such as language differences and customer preferences.

<http://ec.europa.eu/COMMFrontOffice/PublicOpinion/index.cfm/Survey/getSurveyDetail/instruments/FLASH/surveyKy/2059>

²⁸ See Flash Eurobarometer 413; See also Eurobarometer 359 (2012), Retailers' attitudes towards cross-border trade and consumer protection. According to this survey more than 4 out of 10 retailers say that the additional costs of compliance with different consumer protection rules and contract law, as well as the potentially higher costs of the risk of fraud and non-payment are important barriers to their cross-border sales (both 41 %). Higher costs due to distance are considered an important obstacle by 38 % of companies, followed by additional costs of compliance with different national tax regulations and higher costs of cross-border delivery (both 36 %). Around one third of companies view potentially higher costs in resolving cross-border complaints or disputes (33 %) and extra costs from after-sales service in cross-border transactions (31 %) as important obstacles. More than one quarter say that the extra costs arising from different consumption habits (26 %) is an important obstacle, while 25 % say the extra costs from language differences (25 %) is an important obstacle to developing their cross-border sales to other Member States.

²⁹ See Flash Eurobarometer 397 (2015), Consumers' attitude towards cross-border trade and consumer protection; see also Flash Eurobarometer 186, 359 and 396.

³⁰ See, for instance, Flash Eurobarometer 397 (2015), Consumers' attitude towards cross-border trade and consumer protection; Consumer market study on the functioning of e-commerce and Internet marketing and selling techniques in the retail of goods, by Civic Consulting of 9 September 2011, see also European Commission, Consumer Conditions Scoreboard, 11th scoreboard, 2015. Available at the following address: http://ec.europa.eu/consumers/consumer_evidence/consumer_scoreboards/11_edition/docs/ccs2015scoreboard_en.pdf

- (16) Similarly to private persons, when companies purchase online, they are mostly concerned that delivery costs are too high (57 %), that resolving complaints and disputes cross-border is too expensive (53 %), and that their data are not well protected in another Member State (44 %).³¹
- (17) However, there are also indications that companies establish barriers to cross-border online trade through contractual provisions or concerted practices that limit the ability of retailers or service providers in one Member State to serve online customers located in another Member State. For example, according to a 2015 Eurobarometer report³², 16 % of companies that sold online in 2014 or tried to do so indicate that the existence of restrictions imposed by their suppliers on selling to customers located in another Member State is a problem (and for 6 % it is a major problem).
- (18) The growth of e-commerce provides for a number of challenges for companies. In particular, customers can review and compare products and prices online with substantially reduced search costs. This increased transparency is even more pronounced with regard to the widespread use of mobile devices for e-commerce. Smartphones and mobile apps are powerful tools for e-commerce growth. New apps also allow customers to scan product codes, compare prices and purchase products online. New distribution methods and models emerge online. For instance companies and customers increasingly use platforms, in particular marketplaces and other intermediaries/price comparison tools.³³ Some companies react to these challenges to existing business models with recourse to vertical restraints.
- (19) Over the last decade certain National Competition Authorities have been particularly active in assessing contractual restrictions in e-commerce. For instance, in 2012 the French Authority conducted a sector inquiry into e-commerce³⁴; while the German, French, UK and other National Competition Authorities carried out several investigations³⁵ into different types of contractual restrictions used in e-commerce. These cases indicate that certain contractual restrictions used in e-commerce have given rise to concerns and warrant closer scrutiny from the Commission in order to ensure effective competition across the EU.

3. THE PURPOSE OF THE SECTOR INQUIRY

- (20) Sector inquiries are investigations that the Commission decides to carry out in sectors of the economy or types of agreements when there are indications that competition may be restricted or distorted within the internal market.³⁶ A sector inquiry is a systematic

³¹ See Flash Eurobarometer 413 (2015), Companies Engaged in Online Activities.

³² *Idem*.

³³ See Flash Eurobarometer 413 (2015), Companies Engaged in Online Activities.

³⁴ Avis n° 12-A-20 du 18 Septembre 2012 relatif au fonctionnement concurrentiel du commerce électronique.

³⁵ For example, see decisions in case CE/9578-12 of 5 August 2013 and of 27 March 2014 ("mobility scooters") of the UK National Competition Authority ("NCA"), decision in case B2-98/11 of 26 August 2015 ("ASICS") of the German NCA, communication of 18 November 2015 ("Adidas") of the French NCA.

³⁶ See Article 17 of Regulation 1/2003.

investigatory tool used to obtain a better understanding of the functioning of a given sector and the types of agreements used in this sector. Sector inquiries do not target specific companies. However, the results of a sector inquiry may point to potentially anti-competitive practices and the Commission may – following a sector inquiry – decide to open case-specific investigations.

- (21) Through the sector inquiry, the Commission seeks to understand how the growth of e-commerce has influenced the choices made by companies regarding the distribution of their products and services and to what extent the growth of e-commerce has led to an increase in contractual restrictions or the emergence of new types of contractual restrictions.
- (22) The sector inquiry is carried out on the basis of requests for information pursuant to Article 17 of Regulation 1/2003 ("questionnaires"). Such questionnaires were sent to various actors in e-commerce markets in the EU, in relation to online sales of both goods and digital content. The responses to these requests constitute the main source of information for the sector inquiry. The data collected and presented in this Preliminary Report should be read as summaries of the qualitative information obtained from the responses. They are not intended to be read as statistically relevant figures in the strict sense.

4. ANALYTICAL FRAMEWORK

- (23) The following paragraphs outline briefly the relevant analytical framework underlying the analysis of the data gathered in the sector inquiry. The aim is not to provide a comprehensive summary of the possible positive or negative effects on competition of contractual restrictions used in e-commerce but to set the legal and economic background in the light of which the information provided during the sector inquiry will have to be read.
- (24) On the one hand, vertical restraints may affect the market structure and the intensity of competition, mainly through foreclosing markets, softening competition and facilitating collusion. Importantly, and as acknowledged in the Vertical Guidelines³⁷, competition concerns with vertical restraints would normally arise only if there is insufficient competition at one or more levels of the supply chain. Moreover, an important objective which guides any assessment under European competition law is that of achieving an integrated internal market. As a result, the creation of obstacles to market integration is a concern with regard to vertical restraints.
- (25) In relation to goods, the sector inquiry examines the prevalence of certain distribution models, such as exclusive and selective distribution agreements, and contractual provisions limiting the ability of retailers (i) to sell cross-border within the EU, (ii) to sell or advertise online, (iii) to sell on marketplaces, (iii) to use price comparison tools, and (iv) to set the retail price freely. Such provisions may restrict competition and may

³⁷ Guidelines on Vertical restraints, OJ C 130, 19.5.2010, p.1

lead to the partitioning of the internal market in breach of the EU competition rules. A detailed assessment of the different restrictions and the applicable legal framework is presented in the sections dedicated to the specific restrictions.

- (26) In relation to digital content, the sector inquiry investigates the presence of territorial restrictions and geo-blocking in the online distribution of digital content. The sector inquiry also examines the prevalent copyright licensing models for online distribution and their possible impact on competition, in particular, with respect to market entry and the possibility of developing new business models or new services. The focus is on exclusive licensing, which under certain conditions, could raise concerns of input foreclosure and the resulting reduction of competition at the distribution level.³⁸ Exclusive licensing may also raise concerns about exclusion of actual or potential competing distributors at the distribution level.³⁹ The issue of access to digital content and potential exclusion of digital content providers is particularly important given the nature of digital content distribution, where offering certain (premium) content may be necessary in order to attract customers.
- (27) On the other hand, vertical restraints may benefit customers, mainly, but not only, through allowing companies along the supply chain to internalise external effects arising either vertically (between a supplier and its distributors) or horizontally (between distributors or between suppliers). Vertical restraints may also reduce transaction costs, avoiding hold-up in case of relationship specific investment and alleviating capital market imperfections.⁴⁰ Dynamic considerations related to investments in the creation of new products may also be relevant for the assessment of certain vertical restraints.⁴¹
- (28) Vertical externalities arise because of the complementary nature of the role of suppliers and distributors in the process through which goods and services reach customers. The decisions and actions taken at the different levels of the supply chain determine aspects of the product offering such as price, quality, service level and marketing, which affect not only the company taking the decisions but also its commercial partners at other levels of the supply chain.

³⁸ For instance, a supplier may have an incentive to employ exclusive licensing in order to resolve the so-called "commitment problem" and increase its profits, while limiting competition among distributors to the detriment of consumers. The "commitment problem" refers to a situation where a supplier with market power may not be able to exercise it because he cannot credibly commit vis-à-vis distributors not to behave opportunistically and offer rival distributors better trade conditions. Therefore, in the absence of a credible commitment mechanism, the supplier cannot exploit his market power, which leads to lower prices. Conversely, by allowing the supplier to commit not to deal with rival distributors, exclusive licensing may negatively affect consumer welfare.

³⁹ See paragraph 156 of the Vertical Guidelines.

⁴⁰ See also paragraphs 106-109 and 225 of the Vertical Guidelines regarding the positive effects of vertical restraints.

⁴¹ This may be a consideration, for example, with respect to audiovisual content creation to the extent that it is characterised by high sunk costs and uncertainty. The incentives to innovate and create new content may be insufficient absent the prospect of obtaining sufficient return. Copyright protection is a means to remedy this problem.

- (29) For instance, retail investment in assuring a particular quality or brand image and, more generally, the offering of demand enhancing customer services, such as promotion, pre-sale advice by specialised selling staff, or post-sale assistance, do not only benefit distributors but also their suppliers. However, a distributor deciding independently on the level of such services will not take into account the profits accruing to the supplier from each additional sale or from maintaining a reputation for high quality. Hence, he may choose a suboptimal level of these services from the point of view of the supplier and, under certain conditions, also from the point of view of customers. Similarly, independent retail price setting may lead to higher retail prices and lower joint profits compared to a situation where decisions of suppliers and distributors were to be coordinated with a view to maximising their joint profits.⁴²
- (30) Horizontal externalities may arise between distributors of the same product when a distributor cannot appropriate fully the benefits of his (costly) sales effort. For instance, demand enhancing pre-sale services offered by one distributor, such as personalised product advice, may lead to increased sales from competing distributors offering the same product and, thus, create incentives among distributors to free-ride on costly services provided by others. For example, customers may visit a brick and mortar shop to try out a product or obtain other useful information on the basis of which they take the decision to purchase, but then order the product online from a different distributor. The possibility of such free-riding and the respective inability of the distributor that offers customer services to appropriate fully the benefits, may lead to suboptimal provision (in terms of quantity and/ or quality) of such services from the point of view of the vertical supply chain.⁴³
- (31) In the presence of such externalities, suppliers have the incentive to control some aspects of the distributors' operations. In particular, through establishing common ownership of the different levels of the supply chain (vertical integration) or through employing different vertical restraints, suppliers could internalise the abovementioned external effects, increase the joint profit of the vertical supply chain and, under certain circumstances, consumer welfare.
- (32) For example, granting exclusivity or setting up a selective distribution system may be a way for suppliers to alleviate free-riding and to restore the incentives of retailers to increase sales effort. Imposing price restraints could achieve the same objective.⁴⁴ Free-riding concerns among retailers and the need for exclusivity may be particularly

⁴² This situation is normally referred to as the "double marginalisation problem". See also paragraph 107(f) of the Vertical Guidelines regarding vertical externalities.

⁴³ Similarly, free-riding could take place among suppliers, for instance, on their investment in promotion, which may increase the sales of competing suppliers. This may be the case when a supplier invests in promotion activities at the retail premises and the distributor sells also other competing brands. See also paragraph 107(a) of the Vertical Guidelines regarding the free-rider problem.

⁴⁴ See also paragraph 225 of the Vertical Guidelines.

relevant in cases where establishing a new brand or an existing brand in a new market requires substantial (sunk) investments on the retailer side.⁴⁵

- (33) A selective distribution system may also help suppliers build reputation for high quality and convey a desired brand image.⁴⁶ Sometimes it may be important for a supplier to signal its quality through limiting its distribution to certain distributors that have a reputation for selling high quality products only⁴⁷ and this can be achieved, for example, through exclusive or selective distribution.
- (34) Vertical restraints could also be employed to deal with opportunistic behaviour that may arise with the so-called relationship specific investments, i.e. investments that have little value outside the specific vertical relationship.⁴⁸ Once such investment has taken place and to the extent that it is largely sunk, the party which bears the cost of the investment could find itself in a weak bargaining position vis-à-vis its trading partner who may have an incentive to engage in opportunistic renegotiation of the terms of the deal. In anticipation of this, the incentives to invest are likely to be weaker and, therefore, the level of investment may be suboptimal from the point of view of the vertical supply chain. Such situations may arise with respect to investments made both by distributors and by manufacturers. For instance, distributors may have to invest in special retail facilities, which cannot be used for the distribution of other manufacturers' products. Granting exclusivity could be a way for manufacturers to provide sufficient investment incentives to distributors.
- (35) Finally, exclusivity may contribute to the alleviation of problems related to the presence of asymmetric information in the context of capital provision.⁴⁹ Such considerations could be particularly relevant for the digital content sectors, where one may encounter high uncertainty on the demand side and high sunk production costs on the supply side.
- (36) Often the same objective could be achieved through different vertical restraints but their effectiveness in solving the problems mentioned in the previous paragraphs and the extent to which customers benefit will depend on the specific circumstances of the vertical relationship. Different vertical restraints can also play a complementary role, as sometimes the impact of a vertical restraint may be limited when it is employed in combination with another type of vertical restraints.⁵⁰
- (37) The sector inquiry is not case specific and does not aim at assessing in detail whether certain vertical restraints are justified in the context of a particular vertical relationship

⁴⁵ See also paragraphs 61 and 107(b) of the Vertical Guidelines.

⁴⁶ See also paragraph 107(i) of the Vertical Guidelines.

⁴⁷ See also paragraph 107(c) of the Vertical Guidelines.

⁴⁸ See also paragraph 107(d) of the Vertical Guidelines.

⁴⁹ See also paragraph 107(h) of the Vertical Guidelines.

⁵⁰ For instance, exclusive distribution may increase promotion and sales effort but exacerbate a double-marginalisation problem (due to reduced intra-brand competition). Vertical restraints which address double-marginalisation, such as maximum resale price or quantity forcing could, therefore, be employed in parallel to exclusivity. See also paragraph 105 of the Vertical Guidelines.

but rather to provide insights into the relevance of certain factors underlying companies' motivation to employ vertical restraints in relation to e-commerce.

5. SELECTION OF ADDRESSEES: GOODS

(38) The e-commerce sector inquiry is carried out on the basis of responses to questionnaires sent to a large number of companies active in e-commerce.

5.1 Selection of retailers

(39) There is no single data source covering the population of retailers selling online in the Member States. Therefore, for the list of addressees to the retailers' questionnaire, the Commission relied on a number of databases, such as Amadeus⁵¹, Euromonitor⁵² and Veraart Research⁵³, as well as information received from professional associations. The Commission also conducted desk research to verify the relevance of potential addressees of questionnaires and, ultimately, to refine the list of selected addressees.

(40) In order to ensure that the list of addressees included companies of different sizes, and also covered a large part of the market in terms of sales, the Commission followed a two-step approach. First, all companies relevant for the purposes of the sector inquiry and for which contact details could be obtained were selected among the "large" and "very large" companies active under given NACE code contained in the Amadeus database⁵⁴, as well as among the companies contained in the Euromonitor database. Second, a number of smaller companies were randomly chosen for each Member State from the Amadeus database (excluding the "very large" and "large" companies) and the data received from professional associations. For some Member States, a dataset from Veraart Research was also used to cross-check and complement the list of addressees.

(41) The Commission also sought to achieve a broad geographic coverage with a minimum of 20 addressees per Member State. The Commission relied on available Eurostat data to obtain a rough approximation of the distribution of companies selling online across Member States. Specifically, the datasets used contained, per Member State, the total number of companies with at least 10 employees, as well as the percentage of companies having received orders via computer mediated networks, belonging to NACE code G⁵⁵ in 2012. On the basis of these data, the Commission approximated the distribution of companies selling online across the Member States and calculated weights for the 28 Member States.

⁵¹ Amadeus (Bureau van Dijk).

⁵² Euromonitor International (2015), Passport database.

⁵³ Veraart Research (2015), Retail Index. Available at the following address: <http://www.retail-index.com/>

⁵⁴ Companies belonging to NACE code 4791 (Retail sale via mail order houses or via Internet) were considered. Companies on Amadeus are considered to be large and very large if they match at least one of the following conditions: (a) Operating revenue - not less than EUR 10 million (USD 13 million), (b) Total assets - not less than EUR 20 million (USD 26 million) or (c) Employees - not less than 150.

⁵⁵ Wholesale and retail trade, repair of motor vehicles and motorcycles.

- (42) The number of responses received per Member State was then affected by varying response rates in the Member States, the inclusion of additional websites that were reported by addressees to the Commission as well as by spontaneous requests for participation and de-activation of questionnaires for companies that were either never active or no longer active in e-commerce.

5.2 Selection of manufacturers

- (43) The questionnaire addressed to retailers requested a significant amount of data on their business relationships with manufacturers. The responses provided by retailers were useful for selection of the companies to which a "manufacturer questionnaire" was addressed. In addition, the Commission sought to include manufacturers in all the product categories covered by the sector inquiry and to ensure that the major players in those product categories were included.

5.3 Selection of marketplaces, price comparison tools and payment system providers

- (44) Relevant marketplaces and price comparison tools were identified based on information received from professional associations and complemented by desk research. The selection includes the most important marketplaces and price comparison tools in the EU, including both the biggest international players and the most relevant regional ones, covering the sale and price comparison of all products within the scope of the sector inquiry.
- (45) Payment service providers were identified based on information received from professional associations and complemented by desk research. The selection includes players that could provide information about their services in most of the Member States, as well as the most important regional players that offer their services in only one or a few Member States.

5.4 Responses received

- (46) Different questionnaires were sent to online retailers ("retailers"), marketplaces, price comparison tools, payment system providers and manufacturers.
- (47) Questionnaires to retailers, marketplaces and price comparison tools had to be filled out on a per website basis, which means that some companies have received and responded to several questionnaires for each website they operate (in one or more Member States). Each such website specific response is counted separately and included in the number of respondents.⁵⁶ Questionnaires were sent out to companies in all Member States.

⁵⁶ For example, if a company operates a website targeting Germany with a top-level domain ".de" and a website targeting France with a top-level domain ".fr", it was required to fill in two questionnaires. The responses were allocated to the respective Member State.

(48) Table A. 1 shows the number of respondents to the retailers' questionnaire per Member State as well as the number of respondents to the questionnaires sent to other market participants.

Table A. 1: Respondents to the sector inquiry in relation to goods

	Retailers		Retailers
Belgium	29	Lithuania	16
Bulgaria	13	Luxembourg	5
Czech Republic	13	Hungary	19
Denmark	32	Malta	12
Germany	338	Netherlands	46
Estonia	11	Austria	24
Ireland	9	Poland	30
Greece	13	Portugal	18
Spain	38	Romania	14
France	48	Slovenia	18
Croatia	6	Slovakia	9
Italy	82	Finland	14
Cyprus	15	Sweden	36
Latvia	11	United Kingdom	132
Retailers			1051
Marketplaces			37
Price comparison tools			89
Payment system providers			17
Manufacturers/Suppliers			259
Total			1453

(49) Questionnaires were mainly sent to market participants active in the following product categories:

- (a) Clothing, shoes and accessories;
- (b) Consumer electronics (including computer hardware);
- (c) Electrical household appliances;
- (d) Computer games and software;
- (e) Toys and childcare articles;
- (f) Media: books (including e-books), CDs, DVDs and Blu-ray discs;
- (g) Cosmetics and healthcare;
- (h) Sports and outdoor equipment (excluding clothing and shoes); and

- (i) House and garden.

6. SELECTION OF ADDRESSEES: DIGITAL CONTENT

- (50) The part of the sector inquiry related to digital content aims at identifying potential contractual restrictions between suppliers (right holders) and providers of online content services.

6.1 Selection of digital content providers (retail markets)

- (51) The sector inquiry focuses only on companies offering online services as part of, or as the entirety of, their services. At the retail level, i.e. at the level of services provided directly to users, such companies are referred to as digital content providers.
- (52) For the purposes of this Preliminary Report a digital content service is considered as being offered online when it is transmitted using the packet switching protocol standard used on the internet, i.e. TCP/IP, when being delivered to end users' premises.
- (53) The starting point for the digital content provider addressee list was a database comprising more than 2 000 online audio-visual operators across the EU. The list was then narrowed down, with a view to ensuring that the final list of addressees would include the following three categories of providers in each Member State:
 - (a) The most important market operators in each Member State;
 - (b) Any potential recent entrant or operator using innovative business models; and
 - (c) A sufficient number of smaller / local operators.
- (54) Given the nature of digital content services the final list includes a relatively limited number of operators in each Member State which however account for the majority of the audience / market. They are referred to as digital content providers from Member States.
- (55) Some of the operators contacted, have a relatively large cross-border presence, either directly or via subsidiaries. These groups were identified separately and defined as those which have operations in at least five Member States. They are referred to as large groups.
- (56) A number of additional questionnaires were addressed to operators which offer online content through agreements whereby such operators host service providers within a hosting environment with a specific set of characteristics, either via software ("hosting online operator") or via hardware ("hosting device"). A revenue sharing agreement can be part of the relationship between the service provider and the hosting operator, while the relationship with the customer may be directly with the former or with the latter, depending on the specific situation. This category of providers is referred to as hosting operator.

- (57) Respondents belonging to each of the three categories above were chosen on the basis that they offer an online service. The online service did not need to be their exclusive or even main activity. However the questionnaires only refer to the online service and not any other aspect of the companies' offer. A set of questionnaires was sent to providers of VPN⁵⁷ and IP routing services, which are often accessed by users to bypass geo-blocking. Many of these companies are not established in the EU, even though they might provide services to customers in the EU. Therefore the number of respondents was unsurprisingly low for this category.
- (58) Digital content providers were asked to submit information in relation to the following categories of products:
- (a) Films: Feature films and motion pictures;
 - (b) Sports: Sports events and sports programmes, including commentaries;
 - (c) Television fiction: Television comedy, drama and animation series or programmes;
 - (d) Children television: Television programmes and series aimed at children, excluding feature films;
 - (e) News: Television news and current affairs programmes and series;
 - (f) Non-fiction television: Television content other than films, television fiction, children's programmes, news and sports events; and
 - (g) Music: Recorded music, excluding music contained in audiovisual content such as background music in films and television programmes.
- (59) A total of 278 digital content providers submitted information in the context of the sector inquiry, including 6 426 licensing agreements. A further 9 companies offering VPN and IP routing services responded to their questionnaire. Table A. 2 below provides the number of respondents per Member State and by category of respondent identified above.

⁵⁷ Virtual Private Network, i.e. an encrypted communication channel that can be established between two computers or IP-based devices.

Table A. 2: Respondents to the sector inquiry in relation to digital content (digital content providers)

	<u>Content Providers</u>		<u>Content Providers</u>
Belgium	13	Lithuania	2
Bulgaria	5	Luxembourg	1
Czech Republic	8	Hungary	4
Denmark	7	Malta	1
Germany	35	Netherlands	9
Estonia	3	Austria	20
Ireland	2	Poland	9
Greece	5	Portugal	7
Spain	17	Romania	6
France	27	Slovenia	2
Croatia	2	Slovakia	5
Italy	12	Finland	5
Cyprus	1	Sweden	14
Latvia	2	United Kingdom	24
Content Providers			248
VPN and IP Routing			9
Large Groups and Hosting Operators			30
Total			287

6.2 Selection of right holders (wholesale markets)

- (60) Questionnaires were also sent to right holders. Right holders were asked to submit information solely in relation to licensing agreements covering, partly or fully, the rights for digital content services provided online.
- (61) Right holders were selected on the basis of the information provided by digital content providers about their main suppliers and with a view to ensuring a relatively broad coverage across the EU and sufficient diversity across product types.
- (62) Compared to the questionnaires sent to digital content providers, fewer product types were covered in those sent to right holders. In particular, films were excluded in order to avoid any potential overlaps with an investigation into the cross-border provision of films by pay-TV providers⁵⁸ that the Commission is conducting. News and non-fiction television products were also excluded from the questionnaire to right holders, since these products were already amply covered in the questionnaires to digital content providers.
- (63) Right holders were asked information in relation to the following product types:

⁵⁸ See the press release on the ongoing investigation, available at the following address: http://europa.eu/rapid/press-release_IP-15-5432_en.htm

- (a) **Sports:** A sports event, such as a football match, or a set of sports events, such as a football season, which is the object of a broadcast production or productions;
- (b) **Television fiction and children television:** Television series, comedy, drama, or entertainment programmes, excluding feature films, and television programmes and series aimed at children, excluding feature films;⁵⁹ and
- (c) **Music:** Recorded music, excluding music contained in audiovisual content such as background music in films and television programmes.

(64) A total of 53 right holders replied to the sector inquiry and submitted a total of 282 licensing agreements (Table A. 3).

Table A. 3: Respondents to the sector inquiry in relation to digital content (right holders)

	Right Holders
Fiction and Children TV	28
Sports	16
Music	9
Total	53

⁵⁹ Television fiction and children television programmes were grouped together in the results from the data submitted by right holders.

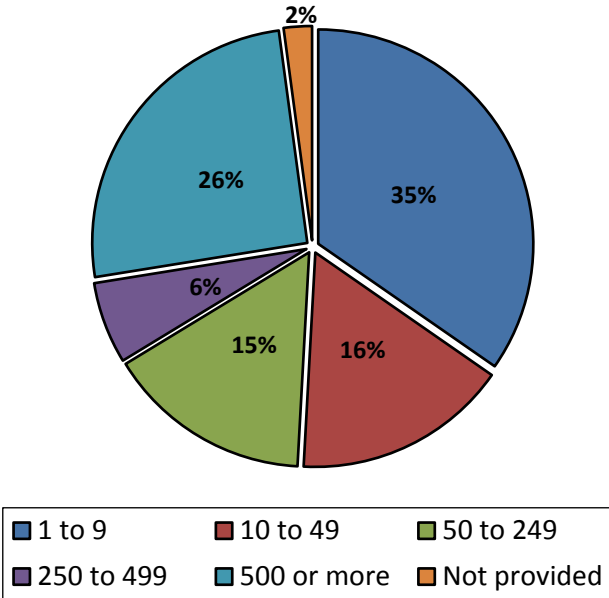
B. E-COMMERCE IN GOODS

1. CHARACTERISTICS OF RESPONDENTS

1.1 Retailers

(65) Overall, the Commission received responses to its questionnaire from 1051 retailers. Respondent retailers cover a wide variety of companies in terms of size, measured either by the number of employees or by the annual turnover generated.⁶⁰ Figure B. 1 shows the distribution of retailers across predefined ranges in terms of the number of employees. About half of the respondent retailers have less than 49 employees.

Figure B. 1: Proportion of retailers by number of employees



(66) 22 % of the retailers generated a turnover of less than EUR 500 000 in 2014, whereas 28 % had a turnover above EUR 100 million, with an approximately equal distribution of retailers of intermediate sizes.⁶¹

(67) Approximately 30 % of the respondent retailers⁶² are also acting as wholesalers and/or manufacturers: 26 % of the respondent retailers are active both at the retail and wholesale level, while 9 % are (also) active in manufacturing.

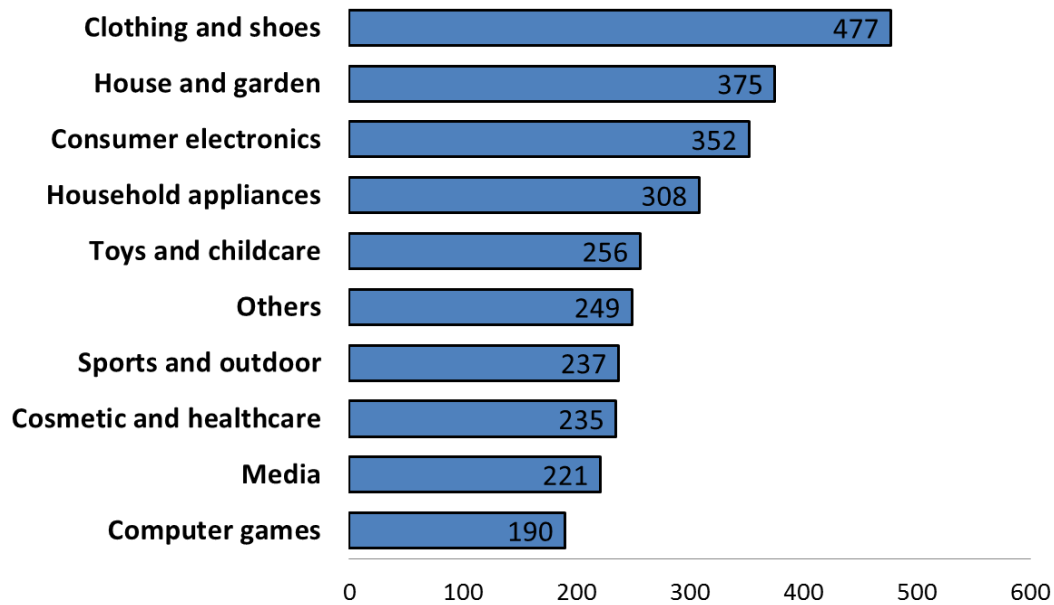
(68) The respondent retailers are mainly active in nine broad product categories (a tenth category covers all "other" products):

⁶⁰ These figures refer to the data provided by the legal entity to which the questionnaire was addressed. As separate questionnaires were sent to different websites of a group of companies, it may occur that some of the respondents reported relatively low figures on the number of employees and turnover in relation to a website that belongs to a larger group.

⁶¹ Based on the total number of retailers (1051).

⁶² 1034 retailers responded to the relevant question.

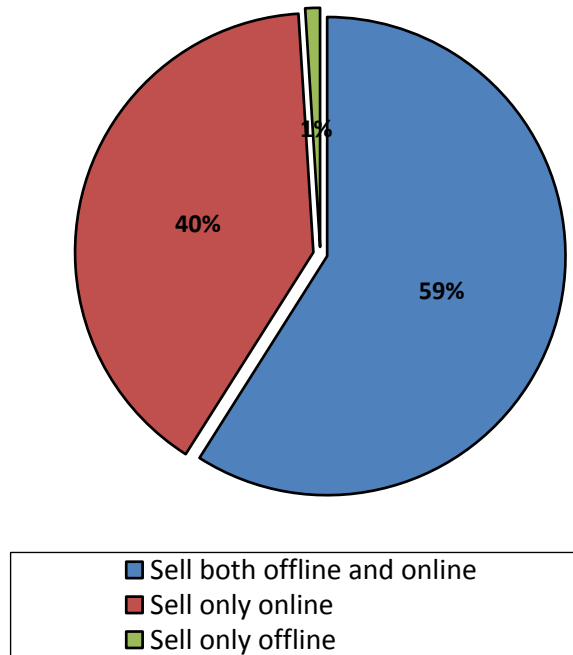
Figure B. 2: Distribution of retailers across product categories (number of retailers)



- (69) A significant number of retailers are active in several product categories: 46 % are active in one product category, nearly 20 % in two categories, 8 % in three categories, 11 % sell products in four or five different categories and more than 15 % sell products in at least six different product categories.
- (70) The majority of respondent retailers are selling both offline and online while a considerable proportion is only selling online without any brick and mortar shop.⁶³

⁶³ 1031 retailers have responded to the relevant question. 1 % of respondent retailers are purely selling offline. This low figure stems from the fact that pure offline retailers were not targeted by the retailers' questionnaire.

Figure B. 3: Proportion of retailers by sales channel, 2014



(71) 92 % of respondent retailers are selling via their own website (which does not exclude that they also sell via other sales channels).⁶⁴ Around a third of respondent retailers are selling via a marketplace⁶⁵ or supply data-feeds to price comparison tools⁶⁶ in order to advertise their products. 38 respondents (representing approximately 4 %⁶⁷ of respondent retailers) were selling online only via marketplaces, i.e. without having their own website. 22 of these respondents were not selling offline. For them, marketplaces are the only sales channel they rely on.

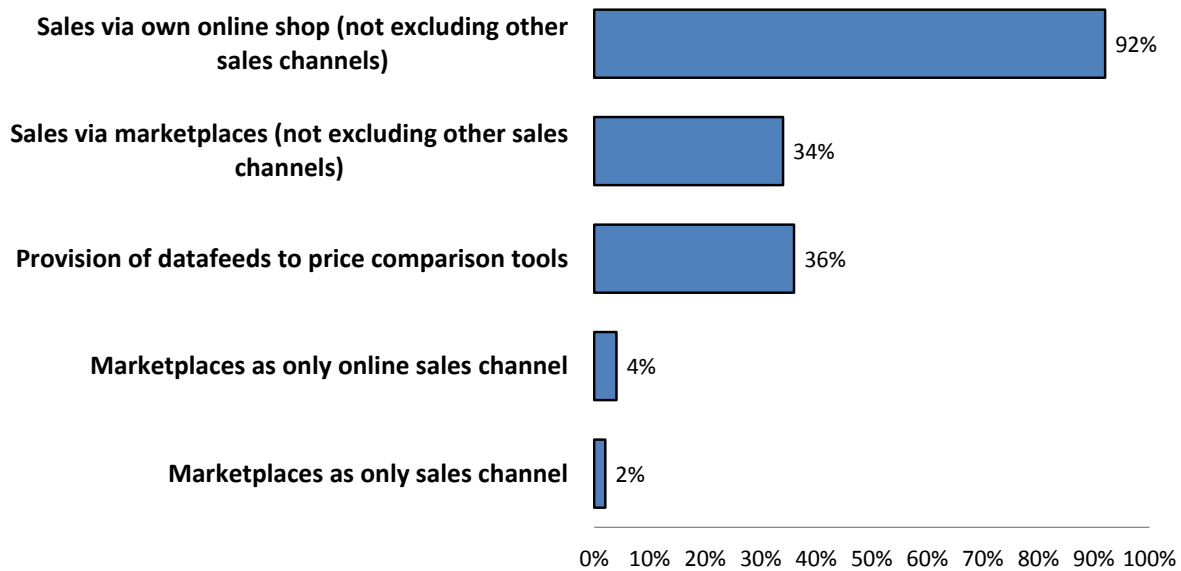
⁶⁴ Proportion calculated out of all 1025 retailers that responded to the relevant question.

⁶⁵ Proportion calculated out of all 1019 retailers that responded to the relevant question.

⁶⁶ Proportion calculated out of all 1013 retailers that responded to the relevant question.

⁶⁷ Proportions are calculated on the basis of the respondents to all relevant questions, namely 1009.

Figure B. 4: Online sales and advertisement activities of respondent retailers⁶⁸



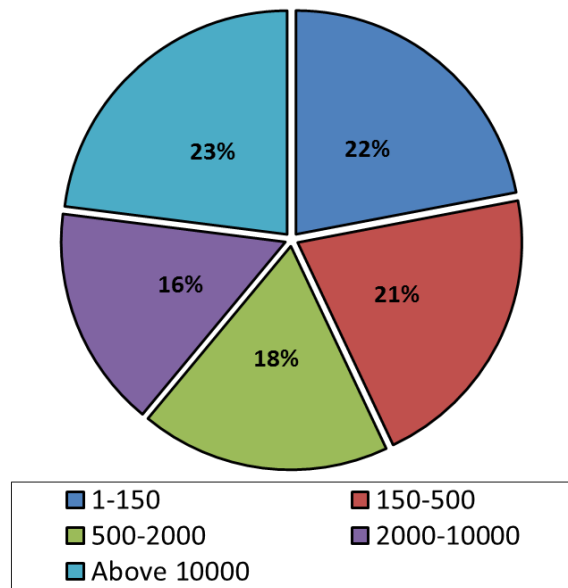
(72) For the purposes of this Preliminary Report, the terms "pure offline players" and "brick and mortar retailers" refer to retailers that only sell in their offline (physical) shop. "Pure (online) players" refers to retailers that only sell online, whether via their own website and/or via third party websites (i.e. marketplaces). "Click and mortar" retailers, "brick and click" retailers and "hybrid" players refer to retailers that sell both online and offline.

1.2 Manufacturers

(73) Respondent manufacturers are evenly distributed in terms of size as measured by the number of employees:

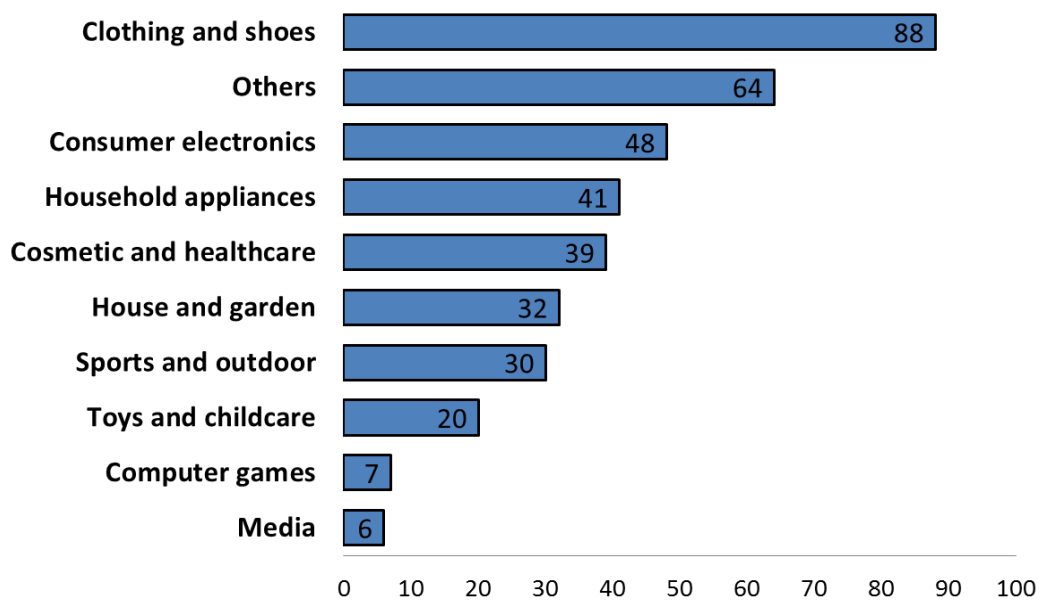
⁶⁸ Note that the percentages for each category presented in the figure have slightly different bases (see footnotes 66- 69).

Figure B. 5: Proportion of manufacturers by number of employees



- (74) In terms of revenues generated in 2014 in the EU, 13 % of respondent manufacturers have a turnover of less than EUR 10 million, approximately 50 % between EUR 10 million and EUR 500 million, and approximately 35 % above EUR 500 million.
- (75) Respondent manufacturers are active in all product categories covered by the sector inquiry, with 26 % active in at least two product categories.

Figure B. 6: Distribution of manufacturers in terms of product categories (number of manufacturers)



- (76) Approximately two thirds of the manufacturers⁶⁹ are also active in the distribution of their products, with a large majority (more than 50 % of all respondent manufacturers) being also active at the retail level.
- (77) For the purposes of this Preliminary Report, in relation to e-commerce of goods, the terms "manufacturers" or "suppliers" refer to both manufacturers that (fully or partially) own the manufacturing facilities and control the manufacturing process, and those that (fully or partially) outsource manufacturing, but own the brand and control distribution strategies.

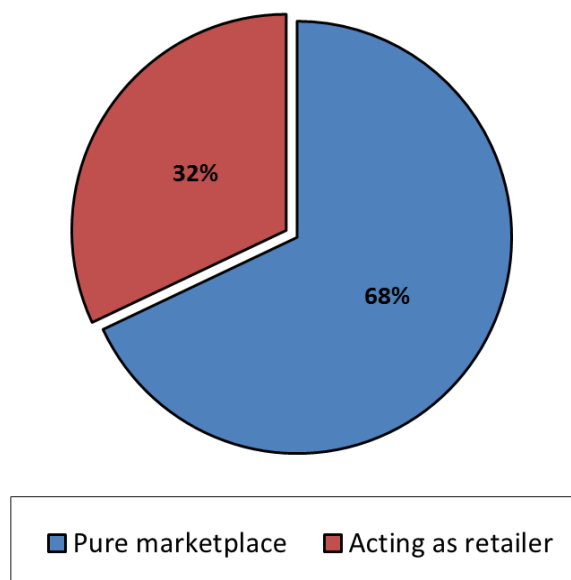
1.3 Marketplaces

- (78) Online marketplaces are multi-sided platforms bringing together different user groups (sellers, buyers and potentially advertisers) and facilitating transactions between them. They allow sellers to list their products on the marketplace and allow buyers of the marketplace to find and buy these products.
- (79) 37 marketplaces responded to the questionnaire addressed to marketplaces. The respondents to the questionnaire operate marketplaces targeting altogether customers in 14 Member States. The Member States which are most targeted by marketplaces are Germany and France.
- (80) The "oldest" marketplaces in the sample were launched in the EU between 1998 and 2001. The marketplaces that were established first tend to be the biggest marketplaces today. Nonetheless, seven respondents launched their marketplaces in 2013 or later. The size of marketplaces varies widely and ranges from marketplaces with a 2014 turnover exceeding EUR 1 billion to marketplaces with a 2014 turnover of less than EUR 100 000.
- (81) The business models followed by marketplaces vary significantly between different marketplace operators.
- (82) Some marketplace operators provide solely the sales platform without engaging in any activity as a seller on that platform ("pure" marketplaces). Other marketplace operators also act as a retailer in addition to offering the sales platform to sellers. In this case, they typically present the products for which they are a retailer together with products of other sellers on the marketplace website. In many cases, they sell the same products in direct competition with those other sellers on the platform. The proportion of third party sales on such marketplaces compared to own retail sales varies from one marketplace to the other and depends to a large extent on the chosen business model of the operator and whether its business started as a retailer or as a marketplace provider. As can be seen

⁶⁹ Within the respondents to the manufacturer questionnaire, there are a few companies that only have wholesale or wholesale and retail activities, but do not manufacture or own the distributed brand(s). Those were not taken into account in these statistics.

from Figure B. 7, out of the 37 respondent marketplaces, more than two thirds are pure marketplaces, while approximately a third also acts as a retailer.⁷⁰

Figure B. 7: Proportion of "pure" marketplaces and marketplaces that act as a retailer



- (83) Marketplaces also differ in terms of the sellers they accept and the selection criteria they apply in relation to sellers. Most marketplaces are open to all interested sellers that comply with basic requirements⁷¹, accept the conditions of the marketplace and are considered sufficiently professional and reliable. However, some marketplace operators do not open their marketplace to all third party sellers. The main business model of these operators is typically that of a retailer. Third party sellers in such "closed" marketplaces are usually sellers whose product range complements the product portfolio offered by the marketplace operator/retailer in question or sellers that pre-existed as suppliers of the marketplace operators/retailer in question. A customer buying a product via a "closed" marketplace will not necessarily know that there is a third party involved in the sale.
- (84) Most marketplaces allow sales of all products, provided that such products can legally be sold and the retailer is able to provide the product information required by the marketplace. A number of marketplaces reported that they only accept new products and do not allow the listing of second-hand products. Some marketplaces do not allow sales of products which are sold under a selective distribution agreement, unless the retailer can prove that he or she is authorised to sell them.

⁷⁰ As marketplaces responded on a per website basis, each website was taken into account separately, even if belonging to the same group of companies. Moreover, a respondent was considered as also acting as a retailer if the retail activity was performed by a different legal entity within the company group of the marketplace operator.

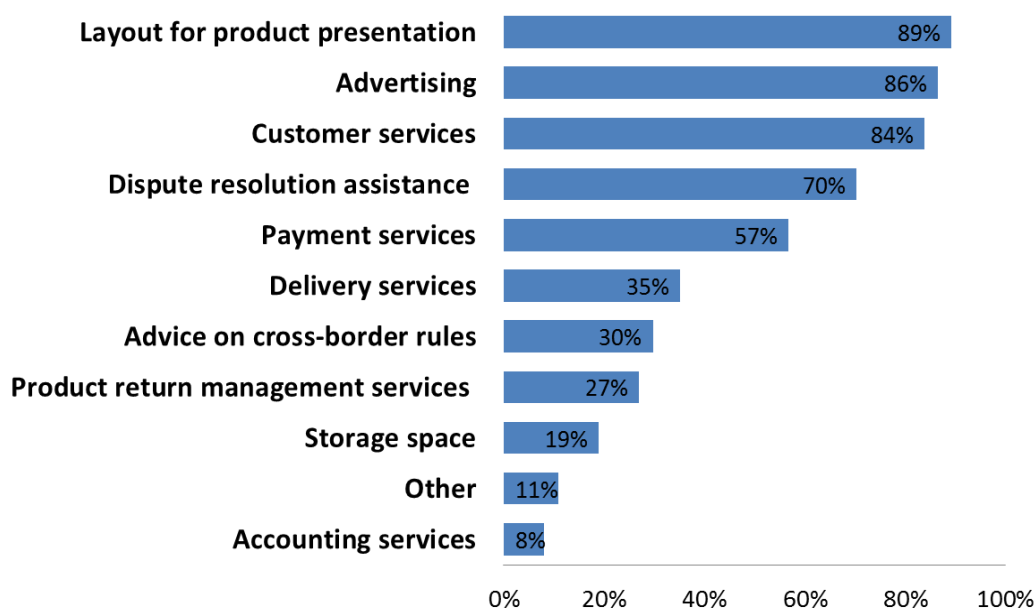
⁷¹ To allow interested parties to register as a seller, some marketplaces require for example the provision of a tax ID, the articles of association, national registration numbers and/or a bank account within the EU.

- (85) There are also a number of differences between marketplaces concerning the contractual arrangements with customers. The party contracting with the customer is not necessarily the third party seller in all marketplaces. Some marketplaces report that they are either separately or jointly with the third party seller contractually liable vis-à-vis the customer. Approximately 8 % of respondent marketplaces indicate that they act as an agent for the seller.
- (86) While, in general, marketplaces established earlier cover a broad range of different product categories, more recent market entrants tend to launch their marketplace to target niche product segments or specific customer groups. Such marketplaces may, for example, specifically target customers in a certain city or region, sellers aiming to get rid of overstock, or specialise in certain product categories or fair-trade products. However, more than 80 % of the respondents report being active in all product categories covered by the sector inquiry.
- (87) Many marketplaces allow sales only by professional sellers, i.e. trading as a business. Some marketplaces offer different remuneration models depending on the intended level of activity of the seller. Others accept also private sellers, i.e. individual persons selling on their own account. On average, approximately 78 % of sellers on the respondent marketplaces are professional sellers, whereas 22 % are either private sellers or sellers which chose a remuneration scheme for limited sales activities.⁷² Some marketplaces have initially started as platforms targeting private sellers and only later opened up to professional sellers.
- (88) The business models of marketplaces also differ in terms of services offered to sellers.⁷³ As can be seen from Figure B. 8, more than half of the respondent marketplaces provide sellers with a standard layout for product presentation, offer advertising possibilities, customer services (including complaints handling), and dispute resolution assistance as well as payment services. Less than a third of the marketplaces that responded to the questionnaire offer delivery services, product return management services or storage space.

⁷² Proportion calculated out of the 30 marketplaces that responded to the relevant question.

⁷³ Such services are not necessarily offered as a separate service by the marketplace, but some of them may form an integral part of the marketplace's offering to sellers.

Figure B. 8: Proportion of marketplaces offering certain services in addition to marketplace function



- (89) Remuneration models also differ between the various respondent marketplaces. Most operators use a fixed (monthly) fee and a per sale transaction fee/commission, which requires the seller to pay a certain proportion of the sales value to the marketplace operator. The level of the per sale transaction fee/commission may differ between different marketplaces as well as between different product categories and the margins achievable by retailers in these product categories. Fee levels are typically lower for consumer electronics than for other products. Some respondents also indicate that they only charge a per sale transaction fee/commission without a fixed fee. Some marketplaces additionally charge a fee per item that is being listed on the marketplace for sale. Rebates offered by marketplaces to sellers take the form of discounts on the per sale transaction fees to either key sellers or to sellers that make use of specific offerings of the marketplace (i.e. top rated seller programs) or sellers that establish a seller shop on the marketplace.
- (90) The majority of the contractual relationships that marketplaces have in place with sellers are based on standard agreements. Only 13 % of the marketplaces indicate that more than 10 % of the agreements they have in force with professional sellers are negotiated individually.
- (91) 86 % of marketplaces report that some of their professional sellers are using third parties for managing their business processes on the marketplace. Such third parties can help sellers to upload their product, inventory and price information on one or more marketplaces, process orders, manage inventory and assist with cross-border trade. They

can provide sellers with easily accessible data on their sales activities across multiple online sales channels.⁷⁴

- (92) Some marketplaces do not only offer a website, but also an app which can be easily accessed with mobile devices such as smartphones.

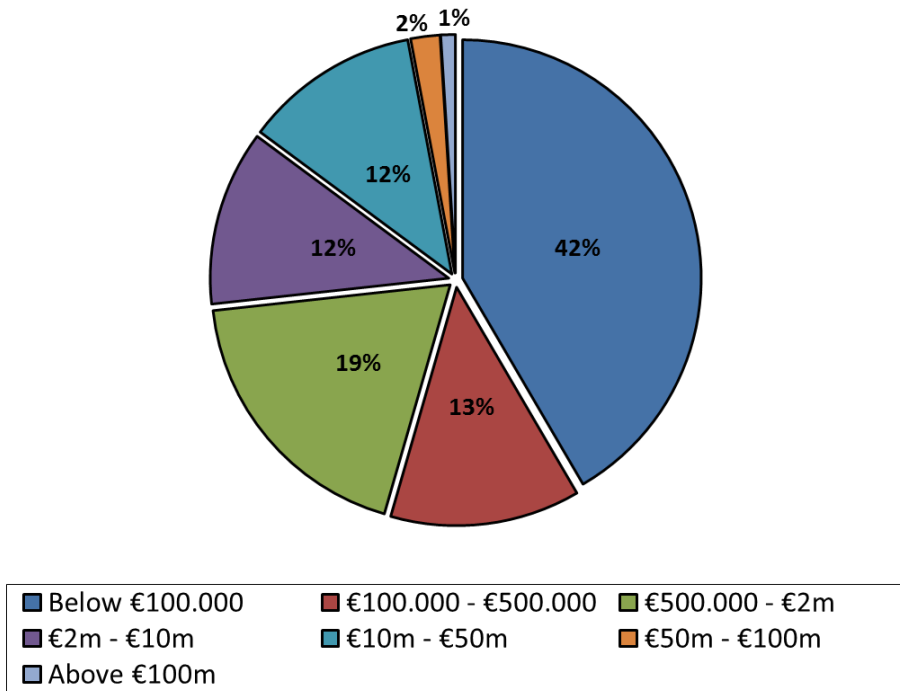
1.4 Price comparison tools

- (93) Price comparison tools are websites/apps that allow customers to search for products and compare their prices across several retailers and provide links that lead directly or indirectly to the product offerings. They do not offer the possibility to purchase the products directly through the website/app of the price comparison tool. Price comparison tools typically do not charge buyers for access to the services on their websites or apps. They are rather financed via payments by the sellers whose products are listed on the websites/apps. Price comparison tools allow customers to quickly compare prices for the same product across a large number of sellers, thereby increasing price transparency and allowing them to find the best available purchase option.
- (94) 89 price comparison tools responded to the Commission's questionnaire addressed to price comparison tools.⁷⁵ The respondents to the questionnaire operate price comparison tools which altogether target customers in 22 different Member States. The Member States which are targeted by most price comparison tools are Germany, UK and France.
- (95) The majority of the price comparison tools each generated revenues below EUR 500 000 in 2014.

⁷⁴ Examples of mentioned intermediaries are Tradebyte, Channel Advisor, magnalister and plentymarkets.

⁷⁵ Addressees were asked to respond separately for each website they operate. Each response is therefore counted separately. Some respondents provided a single response for multiple price comparison tools they operate. In this case, their response was counted only once.

Figure B. 9: Proportion of price comparison tools per total turnover in 2014⁷⁶



- (96) Price comparison tools are rarely specialised in comparing products for specific product categories. 78 % of respondents indicate that they provide pricing information on eight or more of the product categories covered by the sector inquiry. Almost all respondents provide pricing information in relation to consumer electronics (98 %) and household appliances (97 %), followed by computer games (94 %) and cosmetics and healthcare (82 %).
- (97) The "oldest" price comparison tools in the sample were launched between 1997 and 1999. Price comparison tools normally do not require a registration of the customers and they can easily move from using one price comparison tool to another.
- (98) Business models of price comparison tools differ considerably in terms of remuneration schemes, additional features such as product reviews and methods of data collection on product offerings.
- (99) The majority of price comparison tools finance themselves via per unit charges to sellers. As can be seen from Figure B. 10 most respondents operate on a pay-per-click basis⁷⁷ whereby sellers are charged each time a customer is re-directed to the seller's website. The majority of respondents indicated that they (also) charge fees on a pay-per-sale/order basis.⁷⁸ Such fees often represent only a small proportion of the income of the respective price comparison tools and are frequently only applied to sales by a limited

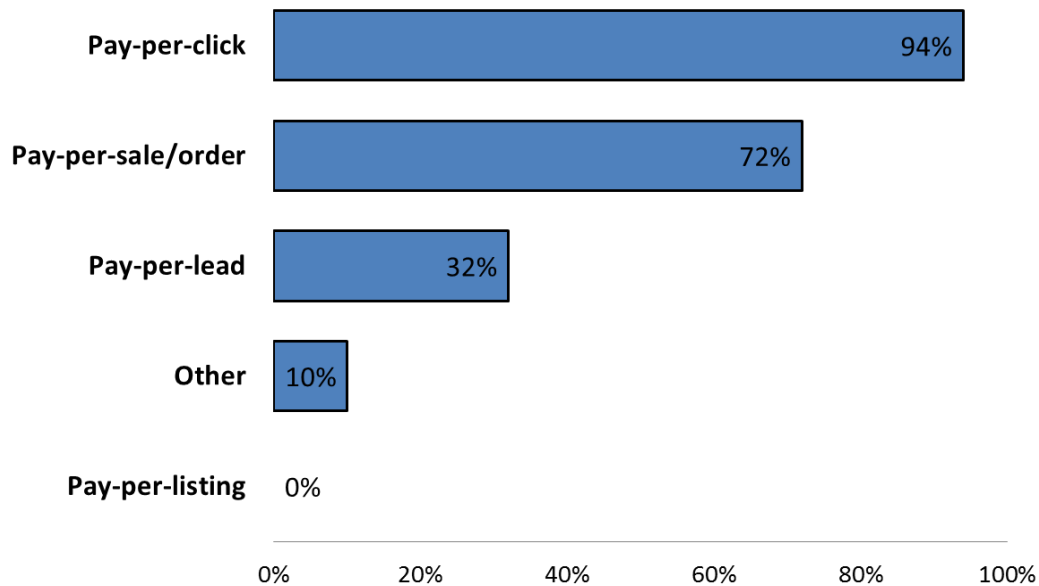
⁷⁶ Proportions are calculated out of 86 respondents that responded to the relevant question.

⁷⁷ Often referred to as cost-per-click (CPC).

⁷⁸ Often referred to as cost-per-acquisition (CPA).

number of important sellers. Per unit charges typically differ between different product categories, reflecting the different profit margins of the products. Some respondents also charge fixed monthly fees to the sellers or allow them to bid to improve the placement of their products on the price comparison tool. Only a quarter of the respondents offer rebates to the sellers that list their products on the price comparison tool (such as volume discounts or free listings).

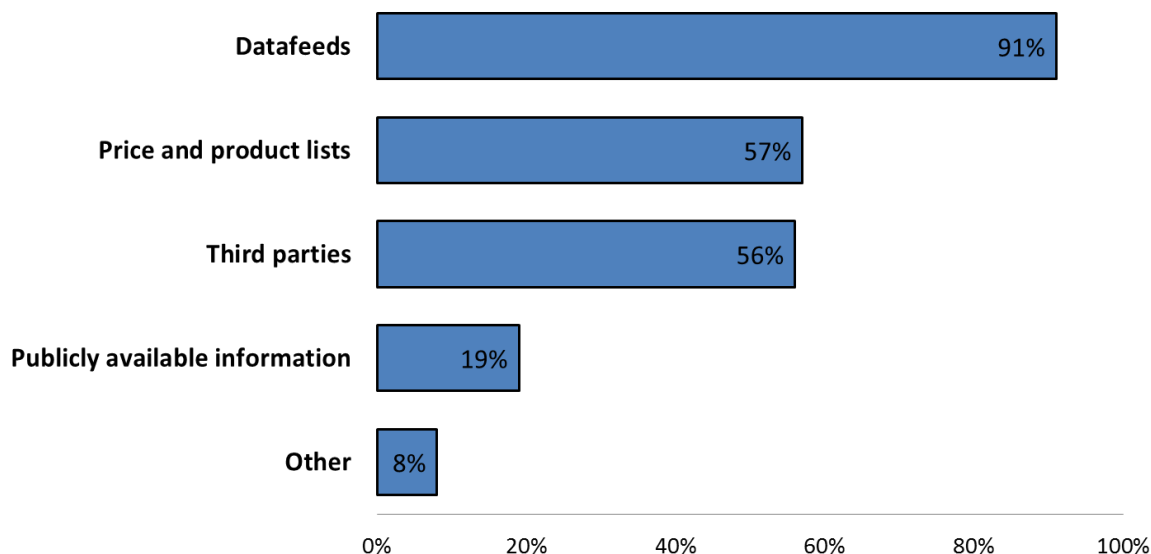
Figure B. 10: Per unit charges applied by price comparison tools⁷⁹



(100) There are a number of ways in which price comparison tools obtain the relevant product and pricing information which is displayed on their website/app. 9 out of 10 price comparison tools indicate that they receive relevant data feeds from the sellers. The majority of price comparison tools also source data from third parties which consolidate information from various sources. Some respondents also use publically available information (e.g. crawling and indexing seller's websites) on product offerings and prices.

⁷⁹ Proportions are calculated out of 81 respondents that answered the relevant question.

Figure B. 11: Collection of relevant information by price comparison tools⁸⁰

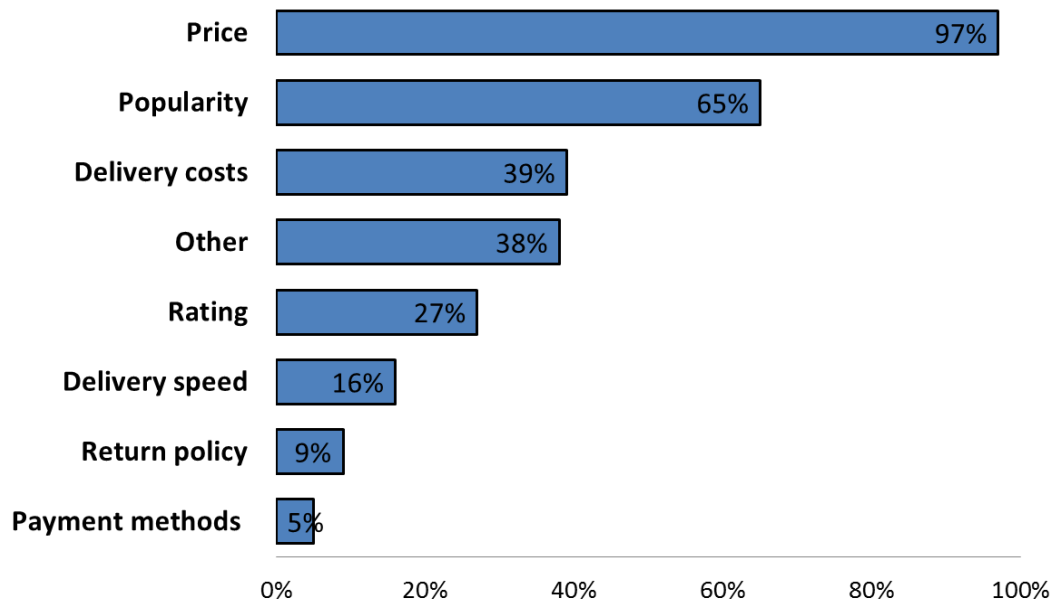


(101) Price comparison tools frequently offer a number of other services to customers next to the price comparison function. These include, for example, customer reviews concerning products or web shops, professional product reviews, information on price history, price alarms and newsletter functionalities. Some operators also offer the possibility to ask product related questions or create lists of favourite products. Additional services which price comparison tools offer to sellers include provision of performance data, premium placement of offers, or advertising.

(102) As can be seen from Figure B. 12, price comparison tools often offer a range of possible product ranking criteria, the default ranking usually being according to price.

⁸⁰ Proportions are calculated out of 88 respondents that answered the relevant question.

Figure B. 12: Proportion of price comparison tools offering certain ranking criteria⁸¹



(103) Price comparison tools usually accept listing products if they fall within a tool's product category catalogue, the seller is able to provide the required information, and the seller is legally allowed to sell the product. Many price comparison tools report that they do not accept listing second hand goods. Price comparison tools typically also verify whether the seller's website is trustworthy and complies with basic legal obligations.

1.5 Payment service providers

(104) In total, 17 online payment service providers replied to the relevant questionnaire. The respondents range from large multinationals with a turnover over EUR 1 billion to a small regional player that achieved a turnover of below EUR 2 million in the last financial year.

(105) The value of online purchases that these payment service providers processed for retailers established in the EU grew by approximately 25 % per year since 2012.

(106) In terms of geographic coverage, the majority of respondent payment service providers provide services across the 28 Member States of the EU, and only three respondents serve fewer than 10 Member States.

(107) The main function of payment service providers is to facilitate payments between retailers and customers. For this reason, payment service providers tend to form partnerships with various financial entities in order to cover as many payment methods⁸² as possible. On average, there are approximately 20 different payment methods for e-

⁸¹ Proportions are calculated out of 88 respondents that answered the relevant question.

⁸² For example, payment methods such as different credit and debit cards, giro pay and direct debit.

commerce available via payment service providers, according to the replies received. Some payment service providers accept over 50 different payment methods.

(108) The number of methods payment system providers accept varies from one Member State to another: several payment system providers accept more than 20 different payment methods in one Member State and less than 10 in others.

Summary

Manufacturers and **retailers** of all sizes are represented in the sample both in terms of number of employees and in terms of turnover. Most of the retailers sell products in at least two product categories covered by the sector inquiry, but many sell in more than six. More than half of the respondent manufacturers also sell directly to customers. About one-third of respondent retailers use marketplaces to sell their products.

The business models as well as remuneration schemes of respondent **marketplaces** and **price comparison tools** are diverse. Sales via marketplaces occur directly on the website of the marketplace whereas price comparison tools only re-direct the customer to the website of the seller on which the transaction subsequently takes place. A third of the respondent marketplaces also act as retailers in addition to providing platforms that bring together third party sellers and buyers. Marketplaces as well as price comparison tools typically offer or display a wide range of products to attract customers and most offerings cover multiple product categories.

The coverage of Member States by **payment service providers** is fairly broad, while the number of methods available may significantly vary depending on the Member State.

2. MAIN FEATURES OF COMPETITION IN E-COMMERCE IN GOODS

2.1 The concentration of manufacturers and retailers in the sectors covered by the sector inquiry

(109) Vertical agreements between manufacturers and retailers can limit intra-brand competition, i.e. competition between retailers selling (branded) products of the same manufacturer.⁸³ While this is a question that has to be assessed on a case-by-case basis, the preliminary results of the sector inquiry offer general insights regarding the level of competition in the sectors covered, both at the retailer and manufacturer levels.

(110) In order to approximate the level of concentration of manufacturers and retailers in the sectors covered by the sector inquiry, the Commission requested manufacturers and retailers to name their "most important competitors" in the sectors in which they are active.

⁸³ On the potential negative effects of vertical restraints and, in this context, the importance of inter-brand competition, see paragraphs 100 to 105 of the Vertical Guidelines.

- (111) The main manufacturers are active in the majority of Member States, with the exception of the category of house and garden where most manufacturers are only active in a few Member States. In clothing and shoes, more than 20 manufacturers are mentioned in each Member State, with the same 5 to 10 brands listed throughout all Member States. In the toys and childcare sectors, also the same 5 to 10 manufacturers are typically mentioned as main competitors in all regions of the EU. More than 20 manufacturers are mentioned in consumer electronics, in all Member States, referring largely to the same players. 10 to 20 manufacturers are mentioned in electrical household appliances, and sports and outdoor equipment. Over 20 main brands are mentioned in all Member States in cosmetics and healthcare, with a significant portion of those listed in the majority of Member States.
- (112) At the retail level, in clothing and shoes, consumer electronics, as well as in cosmetics and healthcare, a significant number of retailers are mentioned as main competitors, with however a few retailers being active in nearly all Member States, and the leading (most mentioned) retailers varying from one Member State to the other. In household appliances, computer games and software; and in media, apart from one online player that is active in most Member States, the main retailers differ from one region of the EU to another.

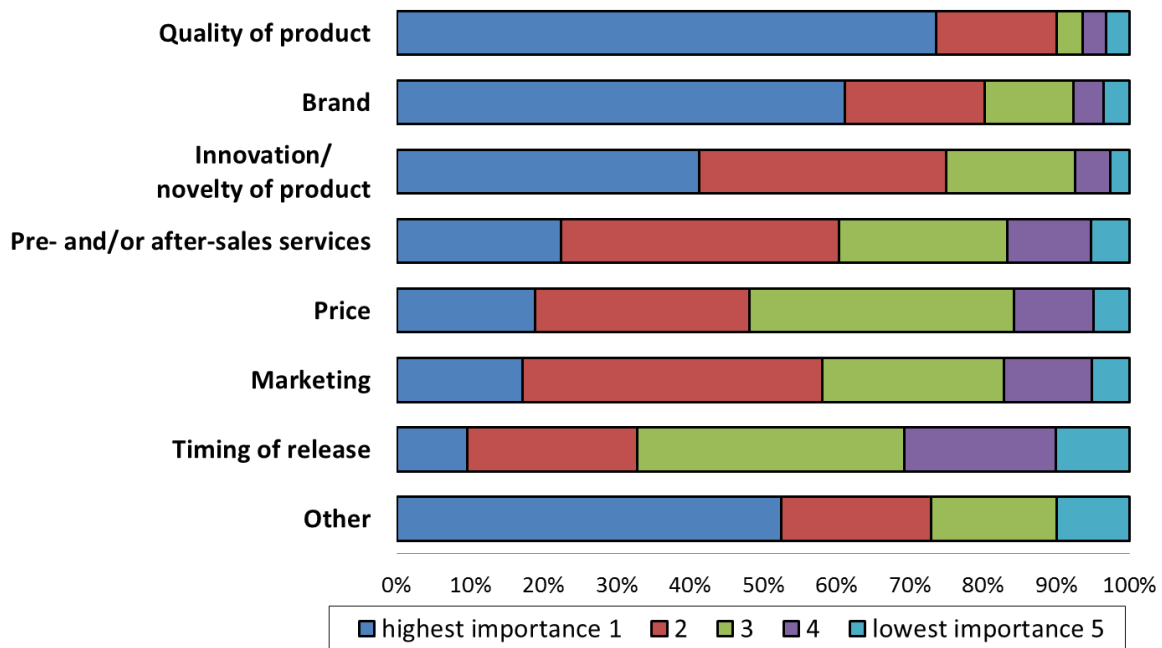
Summary

None of the sectors covered by the sector inquiry seems highly concentrated: the number of manufacturers and retailers perceived as main competitors is significant throughout the different regions of the EU.

2.2 Main parameters of competition

- (113) In order to understand better the competitive landscape in the sectors covered by the sector inquiry, the Commission sought the views of both retailers and manufacturers regarding the importance of various parameters of competition.

Figure B. 13: Rating the parameters of competition by manufacturers⁸⁴



(114) Although there are some differences between product categories in terms of the importance of each parameter, product quality, brand image and the novelty of the product are given the greatest importance by manufacturers in all product categories (with the exception of media products⁸⁵). Ranked on the basis of the proportion of respondent manufacturers that have attached to it the highest level of importance, price only comes at between the fourth and sixth place, with on average only about 20 % of the manufacturers considering it as highly important.⁸⁶

(115) Under "other" parameters, manufacturers mostly stress the importance of the creative / innovative nature, the safety, the design and sustainability, the ease of use of the product, the quality of the distribution network, the individual shopping experience, the ability to offer personalised advice, the satisfaction of individual customer needs, the number of points of sale, the delivery time, the diversity of products and environmental considerations in the production process.

(116) Responses by retailers show a different picture. In particular, ranked on the basis of the proportion of respondents that have attached to it the highest level of importance, price

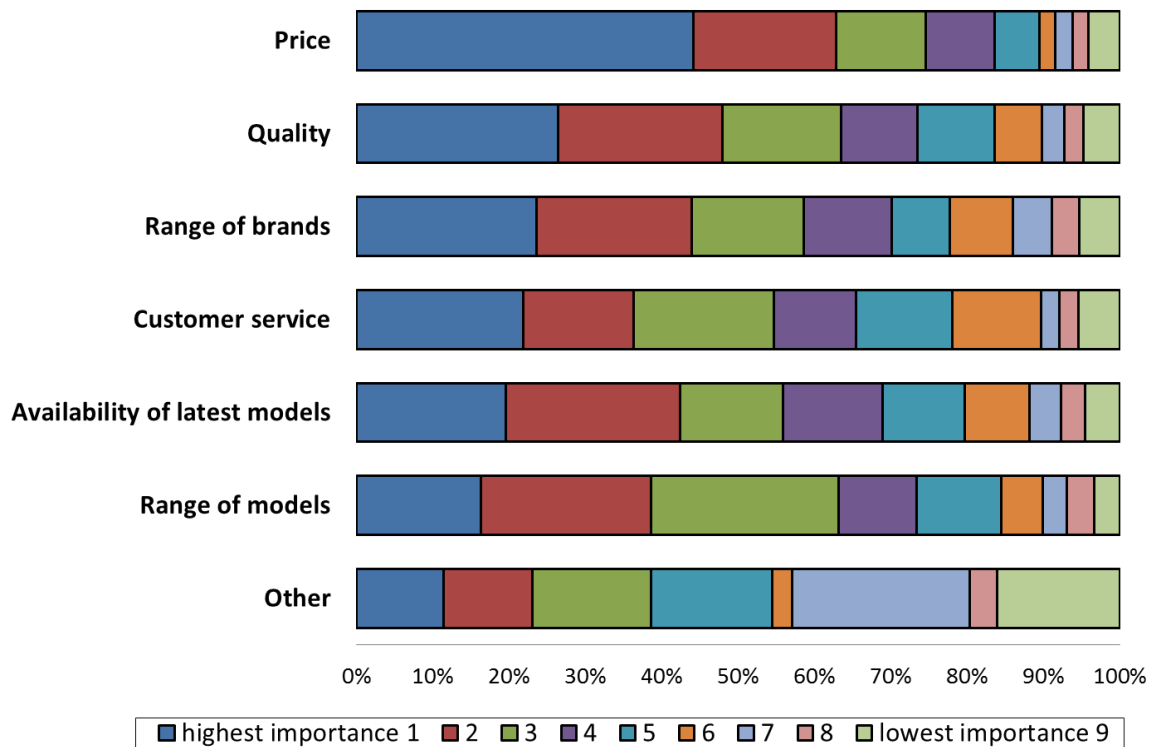
⁸⁴ The proportions presented in the figure are based on the weighted average of the proportion of responses for each product category, where the weights reflect the distribution of responses across product categories. In clothing and shoes, 84 respondents provided the relevant information; in consumer electronics, 48 respondents; in electrical household appliances, 39 respondents; in cosmetics and healthcare, 37 respondents; in house and garden, 30 respondents; in computer games and software, 6 respondents; in sports and outdoor equipment, 26 respondents; in toys and childcare articles, 18 respondents; in media, 5 respondents; and in "other" products, 50 respondents. One respondent may be active in several product categories.

⁸⁵ In the sector of media, novelty was not so highly ranked, but the information is based on only 5 responses.

⁸⁶ Without taking into consideration the category of "other" parameters which refers to various features of competition.

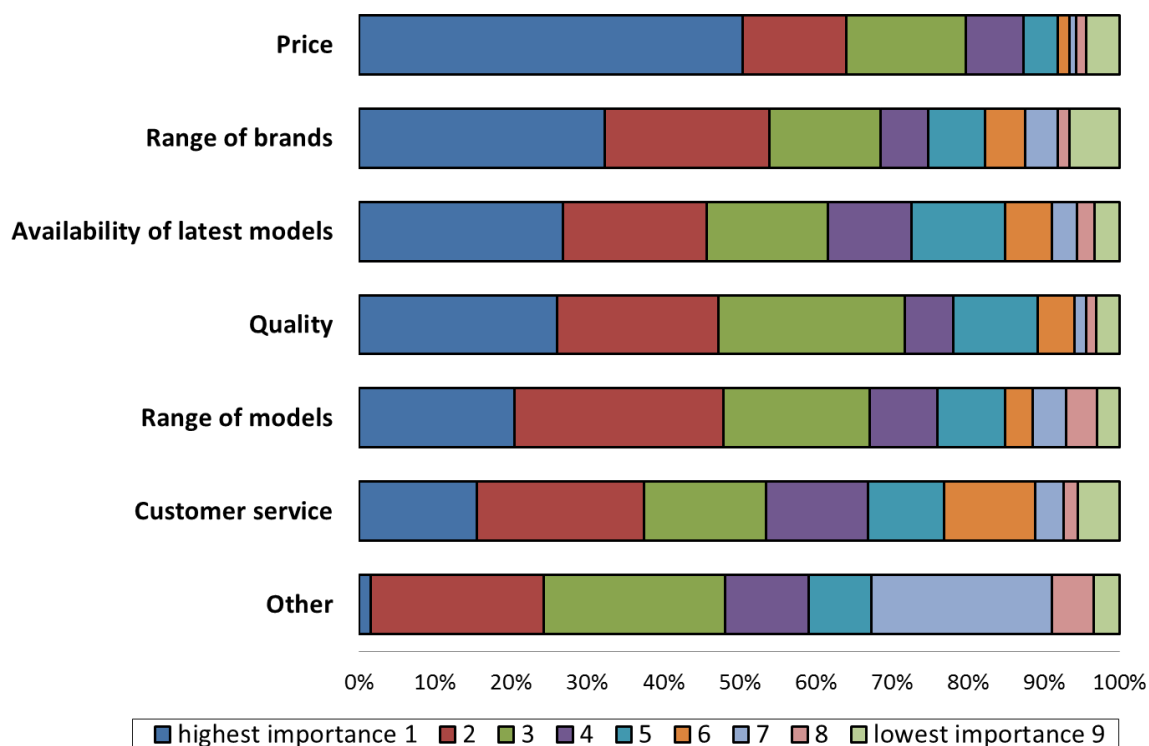
emerges as either the most or the second most important parameter of competition throughout all the sectors. The range of brands, availability of the latest models and quality are the next three most important parameters of competition. However, the importance of parameters varies according to the sales channel the retailer uses. Figure B. 14 shows the responses by hybrid players which operate both offline and online shops, while Figure B. 15 represents the responses by pure online players.

Figure B. 14: Rating the parameters of competition by hybrid players⁸⁷



⁸⁷ The proportions presented in the figure are based on the weighted average of the proportion of responses for each product category, where the weights reflect the distribution of responses across product categories. In clothing and shoes, 259 respondents provided the relevant information; in consumer electronics, 190 respondents; in electrical household appliances, 169 respondents; in cosmetics and healthcare, 129 respondents; in house and garden, 181 respondents; in computer games and software, 92 respondents; in sports and outdoor equipment, 130 respondents; in toys and childcare articles, 125 respondents; in media, 117 respondents; and in "other" products, 84 respondents. One respondent may be active in several product categories.

Figure B. 15: Rating the parameters of competition by pure online players⁸⁸



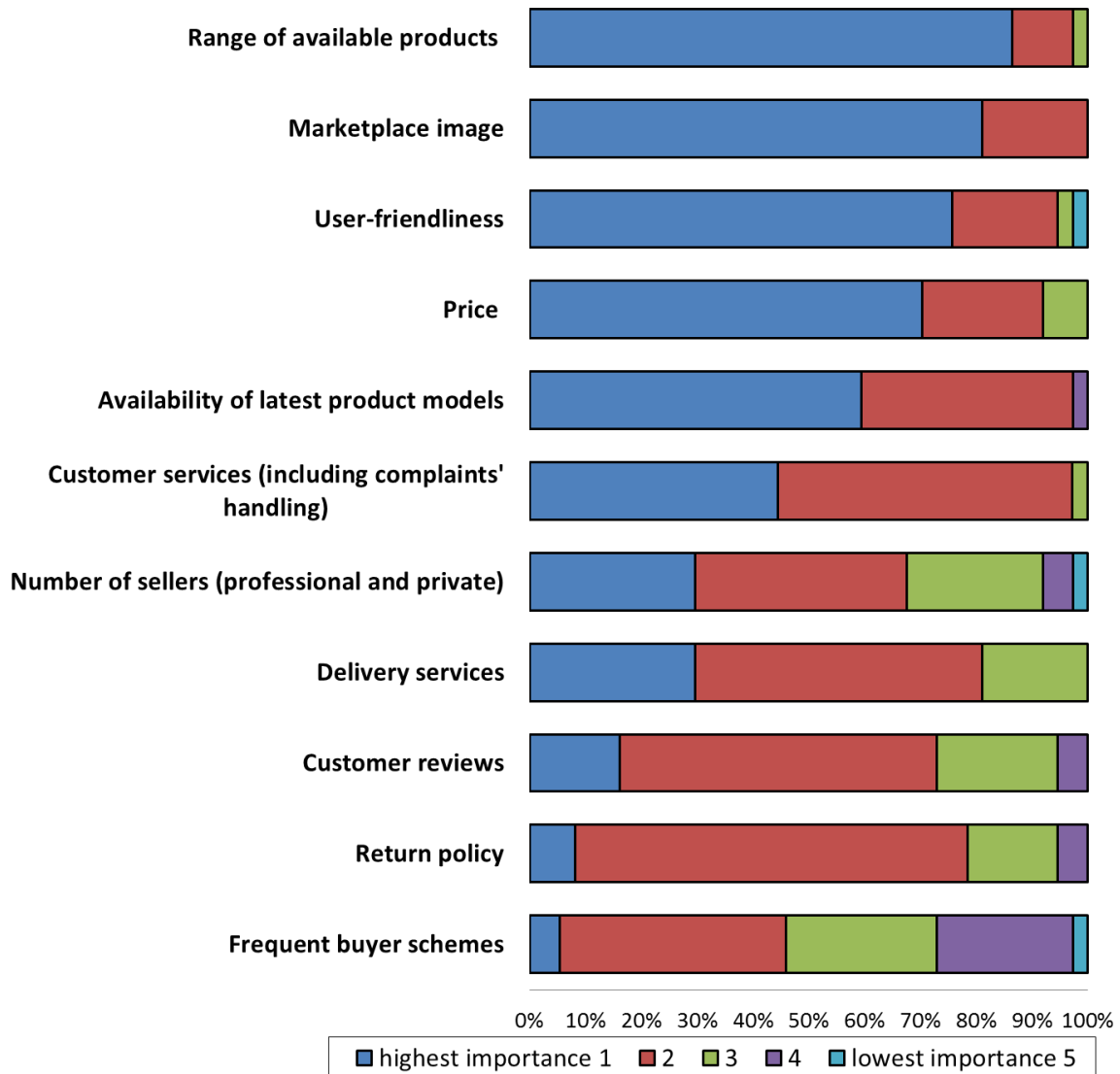
(117) Price is the parameter which is considered highly important by the highest proportion of both hybrid and pure players in nearly all product categories.

(118) However, in terms of proportion of retailers which attach to it a high level of importance, quality is often higher ranked by hybrid players, while the range of brands and/or availability of latest models are typically higher ranked by pure online players. The sector of cosmetics and healthcare is an exception as a higher number of both hybrid and pure online players attach the highest level of importance to quality rather than to price.

(119) Marketplaces were also asked about the importance of various parameters of competition with other marketplaces for buyers. For them, the range of available products as well as the marketplace image and user-friendliness of the website precede price considerations.

⁸⁸ The proportions presented in the figure are based on the weighted average of the proportion of responses for each product category, where the weights reflect the distribution of responses across product categories. In clothing and shoes, 187 respondents provided the relevant information; in consumer electronics, 121 respondents; in electrical household appliances, 95 respondents; in cosmetics and healthcare, 72 respondents; in house and garden, 132 respondents; in computer games and software, 72 respondents; in sports and outdoor equipment, 80 respondents; in toys and childcare articles, 90 respondents; in media, 58 respondents; and in "other" products, 68 respondents. One respondent may be active in several product categories.

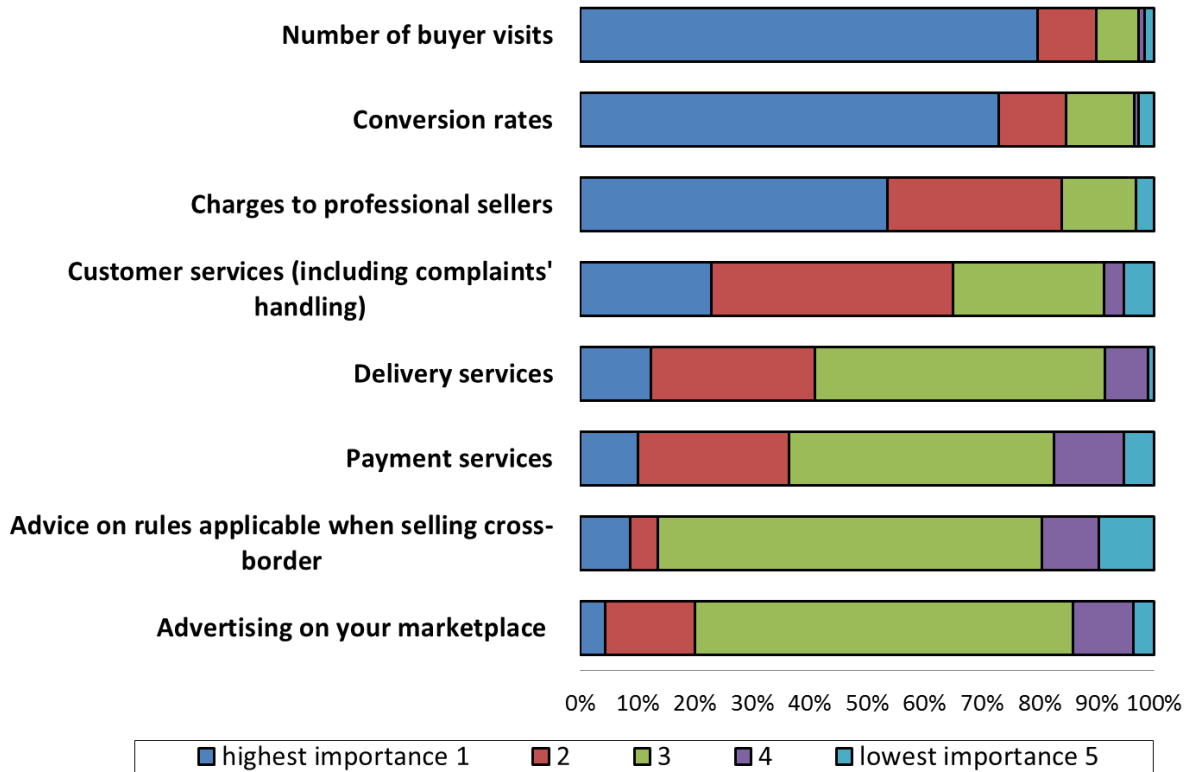
Figure B. 16: Rating the parameters of competition with other marketplaces for buyers⁸⁹



(120) Marketplaces were also asked to indicate the level of importance of a number of pre-defined factors for attracting sellers to their platform. On average, across product categories, the factors to which marketplaces attach the highest importance are number of buyer visits followed by conversion rates and charges to professional sellers.

⁸⁹ Proportions are calculated out of the number of respondents that provided information on the relevance of the respective factor for competition with other marketplaces.

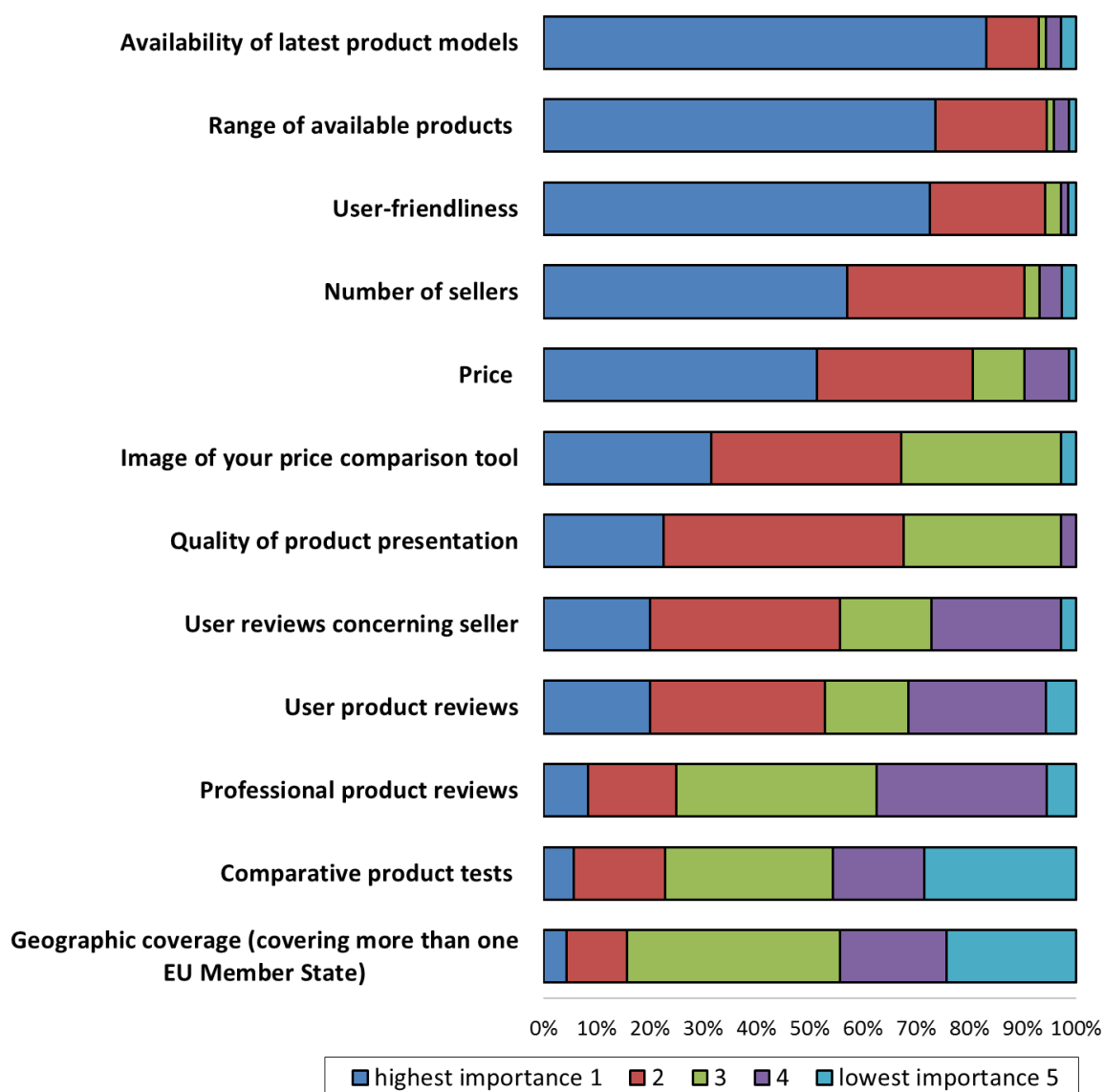
Figure B. 17: Rating the parameters of competition with other marketplaces for sellers⁹⁰



(121) Price comparison tools were asked about the importance of several factors for competing with other price comparison tools for buyers. As can be seen from Figure B. 18, price comparison tools consider the availability of the latest product models as well as the range of available products as important. User-friendliness and the number of registered sellers are factors also considered as important. The ability to be found by important general search engines or popular websites as well as the accuracy of data were several times also mentioned as key factors for competing with other providers.

⁹⁰ The proportions presented in the figure are based on the weighted average of the proportion of responses for each product category, where the weights reflect the distribution of responses across product categories. 33 respondents provided the relevant information in clothing and shoes; 31 respondents in toys and childcare articles and sports and outdoor equipment; 30 respondents in consumer electronics, electrical household appliances, computer games and software and house and garden; 29 in media and cosmetics and healthcare; and 13 respondents in "other" products. One respondent may be active in several product categories.

Figure B. 18: Importance of certain parameters of competition with other price comparison tools for buyers⁹¹



(122) Price comparison tools were also questioned about the importance of several factors in attracting more sellers on their website/app. The factors considered of highest importance by the largest proportion of respondents are the number of customer visits and charges applied to sellers followed by the image of the price comparison tool and the quality of product presentation. Geographic coverage as well as product and customer reviews were considered as less relevant.

⁹¹ Proportions are calculated out of the number of respondents that provided information on the relevance of the respective factor for competition with other price comparison tools.

Summary

Product quality and brand image are considered to be the most important parameters of competition by manufacturers, while price is considered as most important for retailers. Price is the most important parameter for both pure online and hybrid retailers. Quality and range of available brands are the second and third most important parameters for hybrid players, while the range of available brands and availability of latest models are respectively the second and third most important parameters for pure online players. Marketplaces consider the range of available products, the marketplace image, user-friendliness, and the price of products as the parameters of the highest importance for their ability to compete for buyers.

2.3 Pricing

(123) The preliminary results of the sector inquiry show that the increased price transparency online is the feature that most affects the behaviour of customers and retailers. It lowers search costs for customers who are able to instantaneously obtain and compare product and price information online and switch swiftly from one channel to another (online/offline). Manufacturers and retailers are also able to easily monitor prices.

(124) The ability to directly compare prices of products across a number of online retailers, leads to increased price competition, affecting both online and offline sales. The ability to easily compare prices furthers cross-border trade as customers can more easily compare between products or services from different Member States and benefit from price differentials of competing retailers.⁹² Likewise, if a retailer in one Member State is contemplating entering the market in another Member State, this is facilitated by better awareness of the conditions in that market.⁹³

(125) 53 % of the respondent retailers track the online prices of competitors, and 67 % of them (also) use automatic software programmes for that purpose. Larger companies have a tendency to track online prices of competitors more than smaller ones. The majority of those retailers that use software to track prices subsequently adjust their own prices to those of their competitors (78 %).⁹⁴ For more details on price tracking and price adjustments, see section B.4.6.

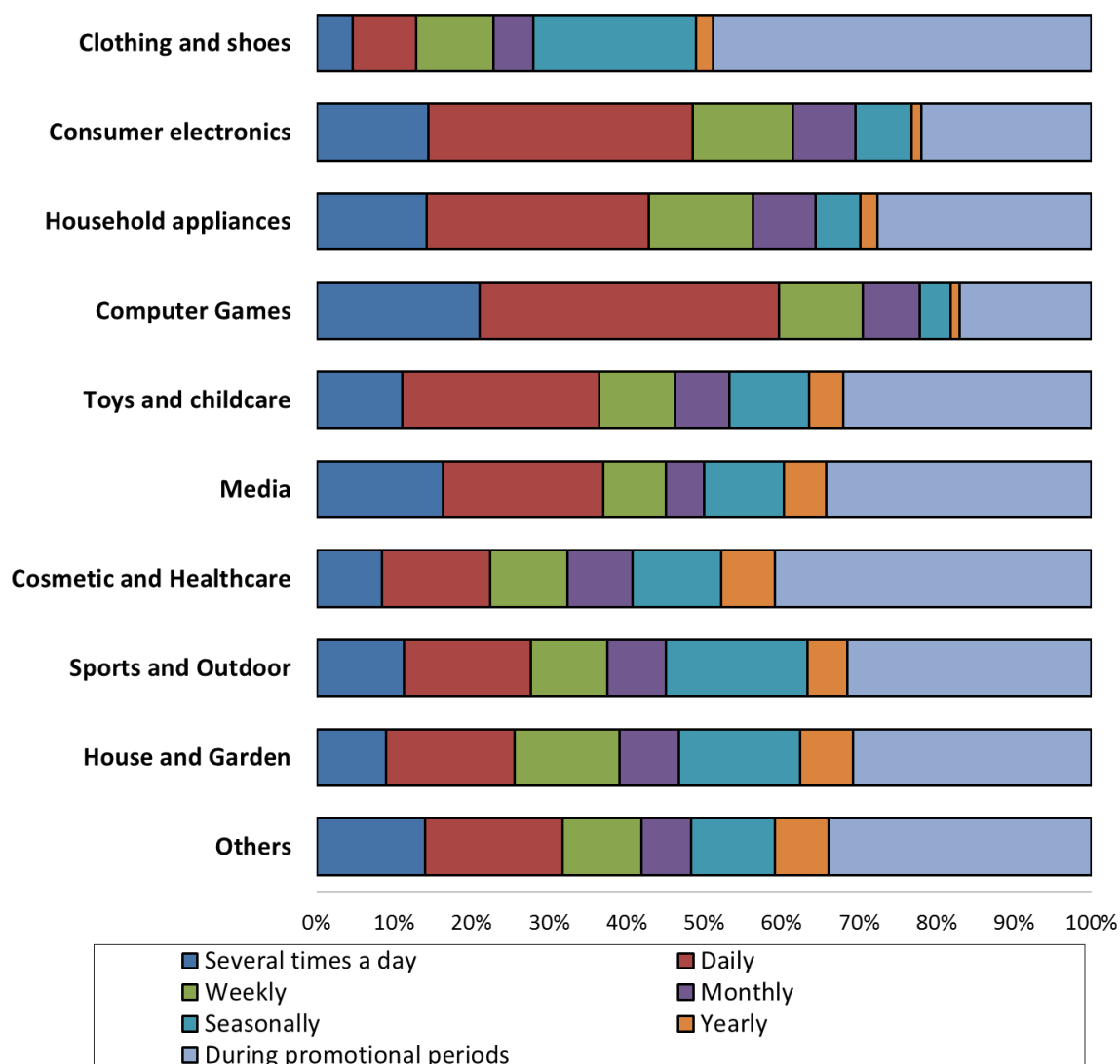
(126) The frequency of online price adjustments depends on the sector, but daily and promotional price changes are reported as the most prevalent ones, as can be seen from the Figure B. 19 below.

⁹² See also submission of the Commission on price transparency to the OECD. Available at the following address: <http://www.oecd.org/competition/abuse/2535975.pdf>

⁹³ Ibid.

⁹⁴ Based on the responses of 343 retailers who responded they were using software to track prices.

Figure B. 19: Frequency of modifying online prices⁹⁵ based on the responses of retailers



(127) Price comparison tools report that daily online price changes are prevalent across sectors, whereas weekly price changes are also frequent. Seasonality plays a role for the category house and garden, and somewhat for sport and outdoor equipment, as well as clothing. Marketplaces indicate that almost one-third of prices change on a weekly basis. Most of them report daily changes for computer games, software and consumer electronics.

(128) Dynamic/personalised pricing, in the sense of setting prices based on tracking the online behaviour of individual customers, is reported as rare. 87 % of the retailers participating in the sector inquiry declare that they do not apply that type of pricing. No pattern in terms of size or profile can be established among the few retailers explicitly declaring that they use or have used dynamic/personalised pricing.

⁹⁵ The figure is based on the responses of retailers who were asked to indicate the most typical price change frequency per sector.

- (129) In order to understand the pricing strategies of the different market players, the Commission requested information on various aspects of manufacturers' and retailers' pricing, and in particular on (a) the differences between online and offline pricing of goods; (b) pricing in case of cross-border transactions; and (c) agreements on pricing between manufacturers and retailers. This section reports on online and offline pricing. The preliminary findings on the latter two issues are set out in sections B.4.3.2.6 and B.4.6 respectively.
- (130) Most hybrid retailers that responded to the specific question (80 %⁹⁶) do not set different prices online and offline. Retailers that do so give diverse reasons for setting different prices. According to their explanation, the response depends among others on the business model of the company. Some respondents see their online business as ancillary to their offline activities. For instance, they sell online only to clear/liquidate stock and therefore set lower prices online. Others have the opposite business model. They are mainly active online and have a few showrooms to complement their online activities. Other respondents do not treat their online and offline activities interdependently and manage their online and offline businesses separately. Finally some of the respondents have a genuine omni-channel approach and consider these channels as parts of one single distribution system.
- (131) The majority of retailers that elaborated on price-level differences explain that their online prices are lower due to more intense price competition online. Others indicate that lower online prices are also due to lower costs, such as the lack of showroom costs and substantially lower pre-sale services' costs. In turn, others suggest that online prices for some products are higher. The main online-specific sales costs retailers mention are delivery costs, platform commissions and payment transaction fees. The main offline-specific ones are high showroom and staff costs.
- (132) The majority of hybrid retailers (70 %⁹⁷) does not achieve different margins online and offline. However, two thirds of the hybrid retailers that charge different prices online and offline⁹⁸ also achieve different margins across the two sales channels and about a fifth of the hybrid retailers that charge the same prices online and offline⁹⁹ also achieve different margins. Half of those achieving different margins charge different prices across the two channels, while the other half do not. The majority of those achieving different online and offline margins indicate that their online margins are lower.
- (133) The preliminary results of the sector inquiry also indicate that any existing price differences between the online and the offline channels cannot be explained by different wholesale prices. Only 26 respondent retailers¹⁰⁰ report that they pay different

⁹⁶ Proportion calculated out of those 513 hybrid retailers that responded to the question.

⁹⁷ Proportion calculated out of those 579 hybrid retailers that responded to the question.

⁹⁸ These are 102 respondents, representing about 17 % of the hybrid retailers.

⁹⁹ These are 411 respondents, representing about 67 % of the hybrid retailers.

¹⁰⁰ They represent only 2.5 % of the respondents.

wholesale prices depending on whether products are meant to be sold online or offline and only half of them pass these differences on through the retail prices.

Summary

Increased price transparency and price competition are the features that most affect the behaviour of market players and customers.

Online prices are adjusted frequently. Retailers increasingly track online prices of competing sellers and many of them react instantaneously to adjust their own prices accordingly. 53 % of the respondent retailers track the online prices of competitors, and 67 % of them use also automatic software programmes for that purpose. Larger companies track online prices of competing sellers more than smaller ones. 78 % of those retailers that use software to track prices subsequently adjust their own prices.

The majority of the respondent retailers do not set different prices online and offline. 70 % of hybrid retailers do not achieve different margins online and offline. However, two thirds of the hybrid retailers that charge different prices online and offline also achieve different margins across the two sales channels.

2.4 Differences between online and offline offers

(134) The Commission also investigated to what extent retailers differentiate their product offering online and offline.

(135) Approximately 70 % of respondent retailers¹⁰¹ offer roughly the same number of brands online and offline. Slightly less than 20 % offer more brands online than offline, while approximately 10 % offer a greater brand choice in their brick and mortar stores.

(136) In terms of models (within the offered brands), 21 % offer a greater choice of models online than offline, while only 6.5 % provide a greater choice of models in their brick and mortar stores.

(137) The main reasons mentioned for offering a greater choice online are as follows: space and stock level constraints in brick and mortar shops (not enough space to show and/or stock all brands and models), competitive pressure by pure retailers to present an exhaustive offer online, marketing reasons (such as avoiding to show models in brick and mortar shops where many sizes are no longer available, whereas the models with "missing" sizes would only be available online as many customers search by size or to clear stock), greater flexibility (easier to add or remove products, change prices, add product-descriptions online, etc.), shipping of products from centralised warehouses allows for easier logistics, complementary nature of offline and online in terms of types of products offered (typically, the more popular brands/models would be sold online

¹⁰¹ Based on the responses of the 606 hybrid retailers who responded to the relevant question.

while the more exclusive ones offline, the older models online while the new models offline).

(138) The main reasons listed by respondent retailers for offering a wider choice in their brick and mortar shops are: less developed website with the desire to keep the core business in the brick and mortar shop (one of the main reasons for this mentioned by the retailers is the quick price "erosion" online/low online profit margins), limits on the sale of certain brands or certain models of a brand (high end products, new models) online, the avoidance of delivery issues, the cost and resource-intensity of maintaining a complete online catalogue.

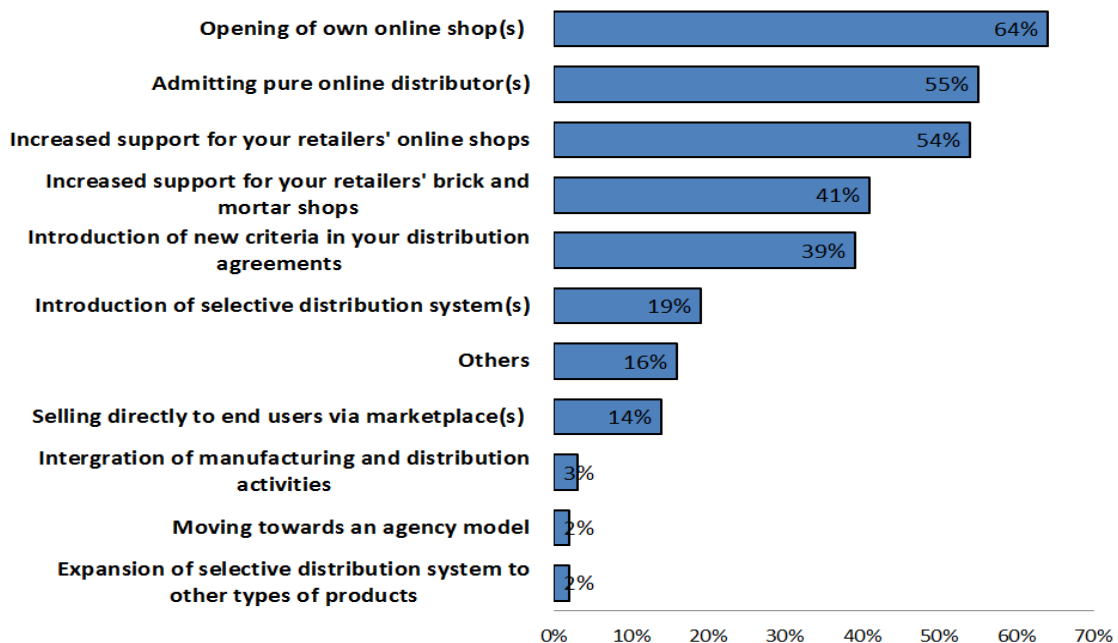
Summary

72 % of the respondent retailers offer an equivalent choice of brands and models offline and online. Approximately 20 % offer a greater choice online while less than 10 % offer a greater choice offline.

2.5 The manufacturers' reaction to the growth of e-commerce

(139) In order to assess the impact of the growth of e-commerce on the business strategies of manufacturers, the Commission inquired about the main measures taken in the last decade to react to this growth.

Figure B. 20: Measures taken by manufacturers in the last 10 years to react to the growth of e-commerce¹⁰²

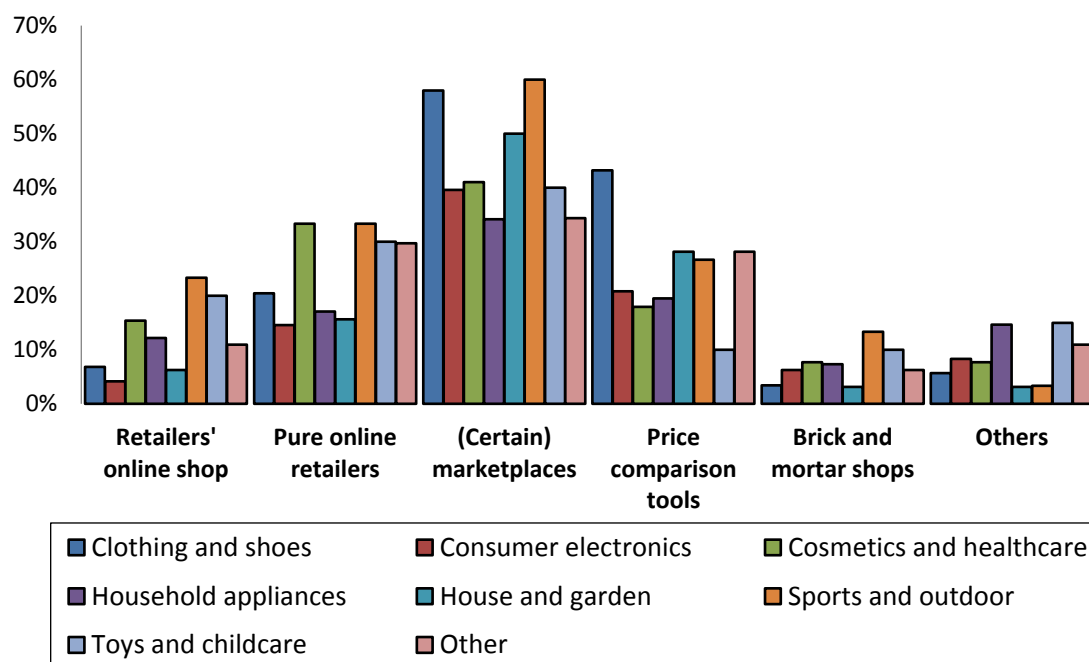


¹⁰² Based on the responses of 244 manufacturers that responded to this question.

- (140) The questionnaires to manufacturers also inquired about the sales or advertisement channels that manufacturers consider as having a potentially adverse or beneficial impact on their business.
- (141) Almost half of the manufacturers that responded to the questionnaire (48 %) indicate that they consider sales via (certain) marketplaces as having a potentially adverse impact on their businesses for at least one of the product categories in which they are active. 32 % of the respondents perceive promotion via price comparison tools to have a potentially adverse impact and 25 % perceive sales via pure online players as having a potentially adverse impact. Only 10 % perceive sales via retailers' website(s) to have a potentially adverse impact on their business (for at least one of the product categories).
- (142) The same picture emerges when looking at the responses per product category.¹⁰³ However, as can be seen from Figure B. 21 there is some variation in the relative importance of each factor across product categories. For instance, while about 60 % of the respondents active in clothing and shoes as well as those active in sports and outdoor equipment, consider that sales through (certain) marketplaces could have an adverse impact on their businesses, only 7 % of those active in clothing but a quarter of those active in sports equipment perceive sales through a retailer's online website as potentially harmful. The opposite is true for the perceived negative impact of promotion via price comparison tools: 43 % of manufacturers active in clothing have pointed to such negative impact in their response as opposed to 27 % of manufacturers active in sports equipment. There are differences across product categories also with respect to the potentially adverse impact of sales via pure online retailers, which are indicated by at least 30 % of the respondent manufacturers in sports equipment, cosmetics, and toys and childcare, and by less than 20 % of the manufacturers in the rest of the product categories (excluding "Other").

¹⁰³ The product categories "Computer games and software" and "Media: Books (including e-books), CDs, DVDs and Blu-ray discs" are excluded from the analysis due to the low number of manufacturers active in these product categories (7 and 6 respondents, respectively).

Figure B. 21: Sales channels viewed by manufacturers as having potentially adverse impact on their businesses, per product category



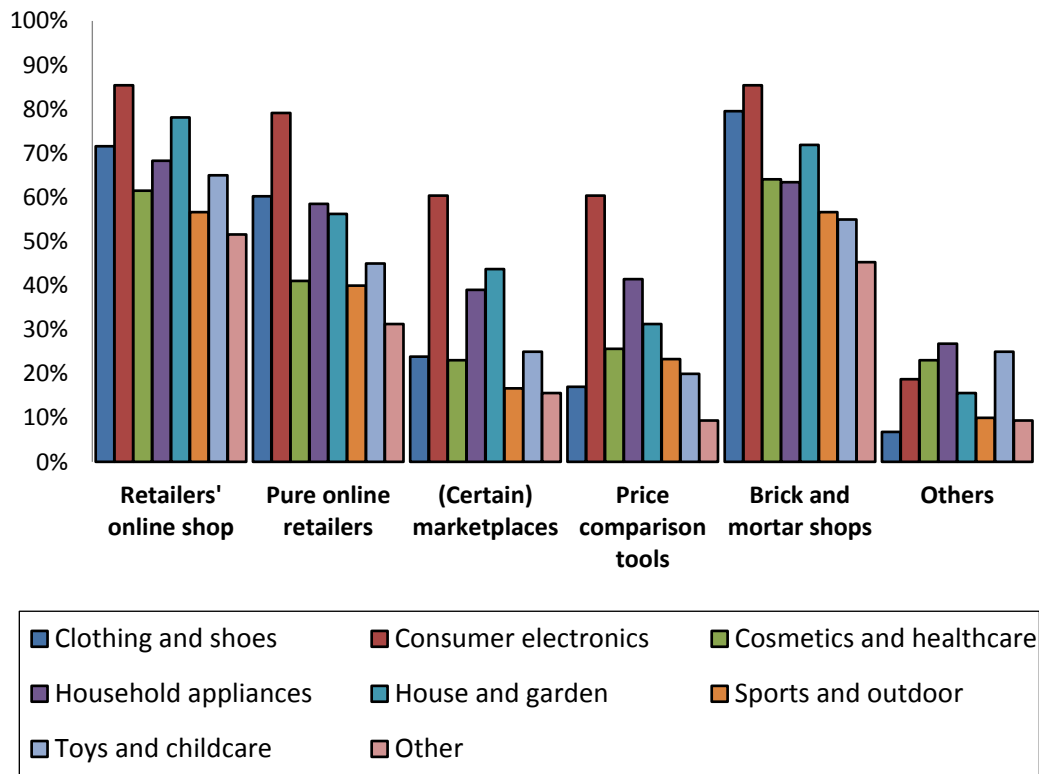
(143) At the same time, the various sales channels are perceived by manufacturers as beneficial for their business, to different degrees. In particular, the great majority of respondents consider sales through retailers' websites as well as sales through brick and mortar shops¹⁰⁴ as being potentially beneficial to their businesses (for at least one of the product categories in which they are active), while 57 % of the respondents think similarly of sales via pure online retailers. Only a third of the manufacturers view sales via (certain) marketplaces as potentially beneficial and less than a third think similarly of promotion via price comparison tools.

(144) Again, there is some variation across product categories as can be seen from Figure B. 22.¹⁰⁵

¹⁰⁴ 73 % and 72 %, respectively, of the respondents to the questionnaire.

¹⁰⁵ The product categories "Computer games and software" and "Media: Books (including e-books), CDs, DVDs and Blu-ray discs" are excluded from the analysis due to the low number of manufacturers active in these product categories (7 and 6 respondents, respectively).

Figure B. 22: Sales channels viewed by manufacturers as potentially beneficial for their businesses, per product category



(145) In internal studies prepared by manufacturers in recent years regarding the effects of the evolution of online sales on their businesses, the following aspects are highlighted most frequently:

- (a) constant price pressure / constraint on the ability to increase prices due to improved price transparency and price awareness / minor price increases may lead to important losses;
- (b) quick online price "erosion";
- (c) constant pressure to make a comprehensive/exhaustive range of products available / need to increase on-shelf availability of products;
- (d) growing importance of keeping uniform, consistent brand image, product and service quality, consistent styles and prices, leading to a growing need for intensified control over distribution;
- (e) growing need for individuality/personalisation;
- (f) increased need for systematic customer relationship management, targeted advertisement, targeted offers/services;
- (g) increased importance of the shopping experience both in brick and mortar shops and online ("website experience");

- (h) growing importance of distribution strategy and quality;
- (i) enhanced competition on delivery terms;
- (j) importance of pre-purchase online search (online product reviews and other product information) throughout the customers' purchasing processes ("shopper journey"), whether the purchases take place online or offline;
- (k) importance of social media;
- (l) free-riding concerns (free-riding by online retailers on the services offered offline and free-riding by brick and mortar stores on the services offered online);
- (m) substantial requests for support both from online and offline retailers and different cost structures for these two sales channels.

(146) Many of the above aspects will be discussed in more detail in the relevant sections of this Preliminary Report.

Summary

As a reaction to the growth of e-commerce, many respondent manufacturers opened their own online shops and/or admitted pure online players to their distribution network. About half of respondent manufacturers consider sales via (certain) marketplaces as having a potentially adverse impact on their businesses for at least one of the product categories in which they are active and only a third of such manufacturers perceive them as potentially beneficial. Online price transparency, quick online price erosion, and the growing difficulties of maintaining a coherent brand image across online and offline channels affect the distribution strategies of manufacturers.

3. DISTRIBUTION

(147) The growth of e-commerce affects the choice of distribution strategies and systems by manufacturers and retailers.

(148) In the context of the sector inquiry, the Commission asked manufacturers, retailers and marketplaces a number of questions about their distribution strategies, the types of distribution agreements used, and the rationale for their choices. In addition, the Commission reviewed more than 2 600 agreements concerning the distribution of goods in the EU.

(149) This section provides the observed trends and explanations regarding distribution, strategies and types of distribution agreements used, with a particular focus on the impact of e-commerce on such strategies.

3.1 Online and offline distribution strategies

(150) Online sales have grown exponentially in the EU since 2000 with an annual average growth rate of approximately 22 %.¹⁰⁶ Given the significant growth of e-commerce and the potential to reach a large number of customers, many manufacturers as well as retailers are keen to make use of new business opportunities by selling online.

3.1.1 Retailers' distribution strategies

(151) Many retailers have embraced online sales and are selling online either in addition to selling offline ("hybrid", "click and mortar", or "brick and click" retailers) or as "pure" online sellers. The majority (59 %) of the 1 031 retailers that responded to the relevant question in the sector inquiry sell goods both offline and online whereas approximately 40 % sell only online without operating any brick and mortar shops.

(152) Some retailers start off as pure online sellers but then expand by opening brick and mortar shops. Out of those respondents that are selling only online, 8 % report that they plan to open a brick and mortar shop within the next two years. The reasons provided for this relate to enabling buyers to pick up products ordered online in a brick and mortar shop or to receiving products from manufacturers that refuse to distribute their products through "pure" online sellers.

(153) While many retailers still have a one-channel focus and use the other sales channel as ancillary, many report about an evolution into a true omni-channel strategy whereby the sales channels complement each other and form part of the same distribution system, with a high level of flexibility for customers to navigate between those two channels back and forth.

(154) Several retailers report about the possibility for their customers to buy online but pick up the products in a brick and mortar shop ("click and collect" option), or the development of online tools in brick and mortar shops to allow immediate online comparison, review and even purchase while being in the brick and mortar store. For instance, some retailers report about their shops offering the direct option of purchasing a product online in their shop in case the product is not on stock.

(155) One example is offering customers to pick up or return the products purchased online in a brick and mortar store.

3.1.2 Manufacturers' distribution strategies

(156) As a reaction to the growth of e-commerce, 64 % of respondent manufacturers¹⁰⁷ launched their own websites within the last 10 years, while 20 %¹⁰⁸ sell products via

¹⁰⁶ Duch-Brown N. and Martens B. "The European Digital Single market", JRC IPTS Digital Economy Working Paper, 2015. Available at the following address: <https://ec.europa.eu/jrc/sites/default/files/JRC98723.pdf>

¹⁰⁷ 244 manufacturers responded to this question.

¹⁰⁸ Proportion calculated on the basis of the responses of 245 manufacturers that responded to this question.

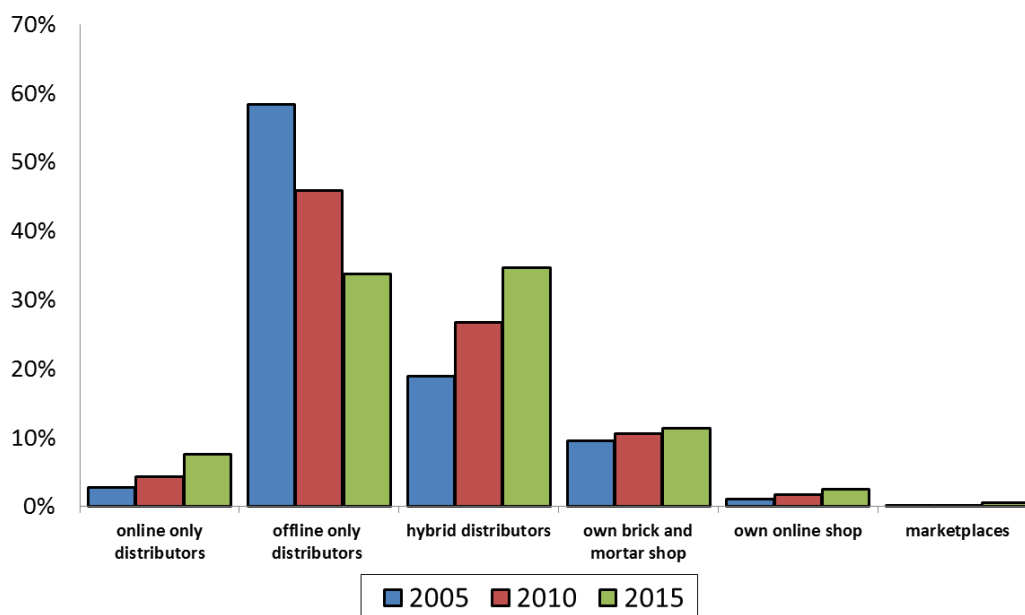
marketplaces and 14 % started to do so in the last 10 years¹⁰⁹. Almost half of the manufacturers (45 %) that answered the relevant question operate their own brick and mortar shops in order to sell their products.¹¹⁰

(157) Manufacturers that own multiple brands do not necessarily report about a uniform distribution policy across Member States and brands. Their strategies may differ from one brand and Member State to another. Most manufacturers however report similar distribution policies as regards distributors selling online and distributors selling offline. Only 7 % of manufacturers indicate that their contractual arrangements differ for independent retailers selling online compared to those selling offline.

3.2 Developments with regard to distribution strategies

(158) In order to analyse the trends in the distribution of products via various online and offline channels, the Commission asked manufacturers for estimates concerning the proportion of their sales through various sales channels in the years 2005, 2010 and 2015.

Figure B. 23: Average proportion of EU sales via the different sales channels¹¹¹



(159) As can be seen from Figure B. 23, the average proportion of sales via independent distributors selling only offline is decreasing, whereas sales via retailers that sell either only online or both online and offline are increasing significantly.

¹⁰⁹ 244 manufacturers responded to this question.

¹¹⁰ Proportion calculated on the basis of the responses of 247 manufacturers that responded to this question. In particular manufacturers active in clothing, shoes and accessories (80 %) and sports and outdoor equipment (54 %) tend to sell their products also via their own brick and mortar shops.

¹¹¹ Proportions are based on the average proportions of sales provided by 238 manufacturers.

- (160) While average sales via self-owned websites only amount to a small proportion (less than 3 %) of the total sales of manufacturers, they have become increasingly important and have on average more than doubled since 2005. Direct sales by manufacturers via marketplaces have multiplied throughout the last 10 years, but still amount on average only to less than 1 % of total sales in 2015.
- (161) The figures show that sales via their own brick and mortar shops have also increased. These are frequently mono-brand stores opened by manufacturers¹¹² in order to promote a specific brand. A new phenomenon is the use by manufacturers of showrooms, usually limited in number, to present their brand(s) which are then sold predominantly online. Increased retailing activities by manufacturers lead to a growing number of manufacturers having entered into direct competition with their own retailer network (see also section B.3.3).
- (162) A number of explanations have been put forward by manufacturers to explain the observed trends. Today, many more customers are willing to buy products online as compared to 10 years ago. The explanations provided by manufacturers on the increasing importance of online sales are mainly the following:
- (a) Increasing customer trust and confidence in online shopping;
 - (b) Faster internet connections coupled with increased computer literacy and the widespread use of smartphones and apps;
 - (c) Accessibility of customers to a wider range of products;
 - (d) Wider geographic reach of retailers;
 - (e) Competitive prices (due to increased price competition and lower cost structures of online retailers);
 - (f) Convenience of a 24/7 shopping opportunity;
 - (g) Timely delivery and the introduction of new delivery methods (such as "click and collect");
 - (h) Establishment of secure payment methods;
 - (i) Traditional offline retailers starting and expanding online sales and engaging in a multi-channel-strategy;
 - (j) Increased support by manufacturers to retailers in relation to their online activities (i.e. trainings, tools, provision of online content);
 - (k) Increased relevance of large marketplaces and pure online retailers;

¹¹² Depending on the business model of the manufacturer, such mono-brand stores may also be operated by third parties (e.g. franchisees).

(l) Improvement of product information available online as well as presentation of content;

(m) Increased quality of services online.

(163) Despite the growing importance of e-commerce, many manufacturers stress the importance of selling their products via brick and mortar shops. In particular, manufacturers of luxury branded goods, such as fashion clothing or perfumes, consider the traditional shopping experience in a specific luxury shopping environment with extensive pre-sale advice to be a central element of their distribution strategy. Some respondents report that the introduction of websites for the sale of certain luxurious brands/products was not successful and disappointing, as customers prefer to purchase high priced products in a traditional luxurious shopping environment.

(164) Manufacturers, however, also report an increased importance of pure online retailers. The majority of manufacturers (64 %¹¹³) sell their products to pure online sellers. 55 %¹¹⁴ of the manufacturers decided to admit pure online sellers to their distribution network in the last 10 years. Conversely, 35 % of manufacturers indicate that they do not sell their products to pure online sellers.¹¹⁵ (For more details on the requirement of having a brick and mortar shop in selective distribution systems, see section B.3.4.3).

Summary

Online sales have grown significantly in the last 10 years. Many manufacturers and retailers are keen to participate in this growth and have expanded selling online.

6 out of 10 retailers that participated in the sector inquiry adopt a multichannel approach selling goods both online and offline whereas approximately 40 % sell only online.

More than half of the respondent manufacturers launched their own websites within the last 10 years as a reaction to the growth of e-commerce. One out of five manufacturers sells products directly to buyers via marketplaces and 14 % started to do so in the last 10 years. Nearly half of the respondent manufacturers sell their products via their own brick and mortar shops.

The proportion of manufacturers' sales via retailers selling only in brick and mortar shops is decreasing, whereas sales through pure online retailers and hybrid retailers are increasing. An increasing part of manufacturers' sales are also achieved through direct sales to customers, both online as well as via brick and mortar shops.

Despite the growing importance of e-commerce, many manufacturers stress the importance of traditional brick and mortar shops. In particular, manufacturers of luxury branded goods, such as fashion clothing or perfumes, consider the traditional shopping experience in a specific

¹¹³ Proportion calculated based on the responses by 249 manufacturers that responded to the relevant question.

¹¹⁴ Proportion calculated based on the responses by 244 manufacturers that responded to the relevant question.

¹¹⁵ Proportion calculated based on the responses by 249 manufacturers that responded to the relevant question.

luxury shopping environment to be a central element of their distribution strategy. Approximately two thirds of manufacturers sell their products to pure online retailers for resale, while one third of manufacturers do not sell to pure online retailers.

3.3 Distribution by manufacturers

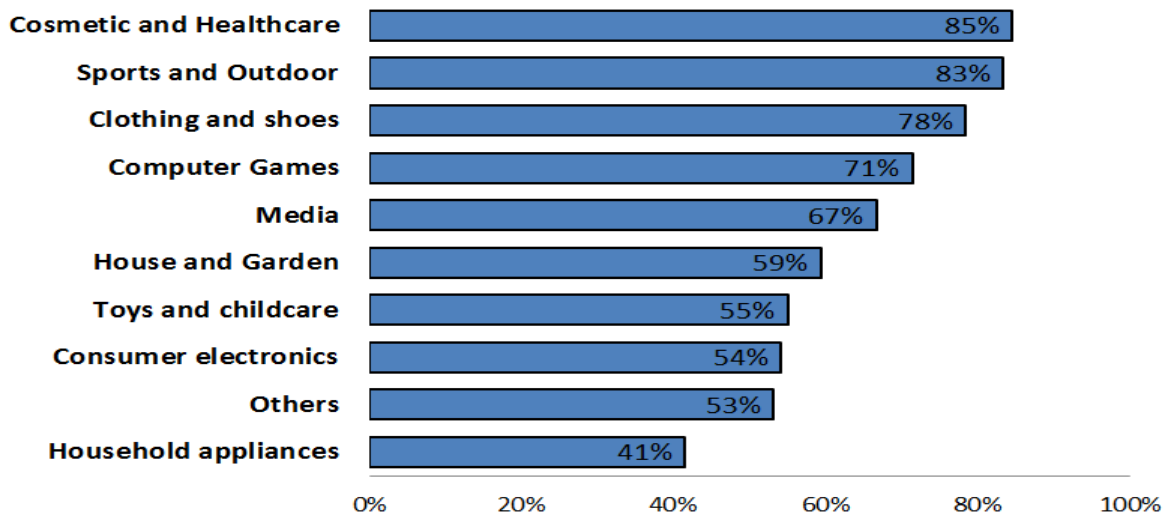
- (165) The analysis in the previous section has shown that an increasing proportion of sales of manufacturers is generated via the manufacturers own retail activities, both online and offline. This suggests increased vertical integration of manufacturing and distribution activities. Vertical integrated distribution occurs where the upstream manufacturing and downstream distribution of the products (both wholesale and retail) is organised within the same company or group of companies - whether run in parallel with an independent distribution network or not.
- (166) As can be seen from Figure B. 20, the most common reaction of manufacturers to the growth of e-commerce over the last 10 years was to open their own online shop¹¹⁶ thereby competing, in many cases, with their own independent retailers. Some manufacturers compete with their own retailers also by operating brick and mortar shops. It is clear that market dynamics of e-commerce have played a key role in pushing many manufacturers to sell their products directly to customers.
- (167) More than two-thirds of the respondents to the manufacturers' questionnaire report that they are vertically integrated as regards at least one other level of the distribution chain, i.e. they are also active as wholesaler and/or retailer.¹¹⁷ The majority (more than 75 %) of these vertically integrated manufacturers indicate that they are active as a retailer.
- (168) The product category with the highest number of vertically integrated manufacturers is cosmetics and healthcare. 85 % of the manufacturers active in this product category are present in at least another level of the distribution chain, closely followed by those active in sports and outdoor equipment where the proportion is 83 %.¹¹⁸

¹¹⁶ See section B.2.5 The manufacturers' reaction to the growth of e-commerce above.

¹¹⁷ Proportions are calculated out of all respondents (259) to the manufacturers' questionnaire.

¹¹⁸ Proportions are calculated out of all respondents (1051) to the retailer questionnaire.

Figure B. 24: Proportion of manufacturers that are vertically integrated, by product category¹¹⁹



(169) Vertical integration of manufacturers however does not necessarily lead to a full elimination of the existing independent retail or wholesale network and the information provided in the sector inquiry suggests that most vertically integrated manufacturers continue to sell also via independent wholesalers and/or retailers.

(170) In addition, a manufacturer may decide to vertically integrate in certain Member States but not in all of them. Manufacturers tend to be present with their own sales force in those Member States that they deem key or strategic while they use independent distributors in others.¹²⁰

(171) Vertical integration has also occurred at the retail level (retailers entering upstream levels of the distribution channel/manufacturing) although to a more limited extent. Approximately 30 % of retailers that responded to the relevant questionnaire reported that they were active also at another level of the distribution chain. Most commonly, vertically integrated retailers act as wholesalers rather than manufacturers.¹²¹

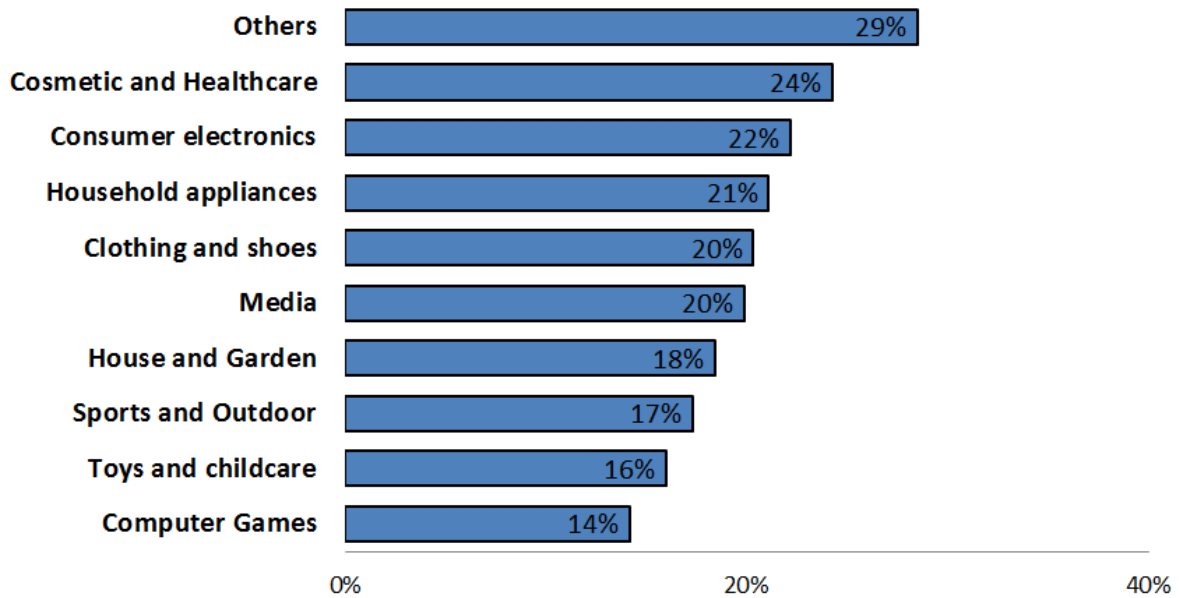
(172) As can be seen from Figure B. 25 below, retailers active in the sales of cosmetics and healthcare products are most likely to vertically integrate (with almost one in four of those retailers present in at least one other level of the value chain), while those selling computer games are least likely to do so.

¹¹⁹ Proportions are calculated out of all manufacturers that are active in each given product category.

¹²⁰ See also section B.4.3.1 *Geographic sales strategies of manufacturers*.

¹²¹ Approximately 26 % of all retailers are also active as a wholesaler while 9 % are active also as a manufacturer.

Figure B. 25: Proportion of vertically integrated retailers, by product category¹²²



(173) Many manufacturers acknowledge that their decisions to vertically integrate are largely due to the fact that, with relatively small investments, they can benefit from the advantages of online sales. Vertical integration also brings increased control over distribution, including both quality and price.

(174) While vertical integration (in the sense of manufacturers engaging in retail activities) may reduce the number of independent retailers, hence, intra-brand competition, it can also streamline the incentives of the manufacturing and the retail level. It may for instance lead to a lower retail price by eliminating double marginalisation. It could also lead to better coordination of pre-and post-sale services.

Summary

Vertical integration of manufacturers, mainly by means of opening their own online shops, is one of the most prominent reactions to the growth of e-commerce. Vertical integration may be a means to reap the benefits of online trade with limited investments and to achieve an increased level of control over distribution, including both quality and price.

By comparison, the proportion of vertically integrated retailers is significantly lower and remains to a large extent limited to the integration of wholesale and retail activities. The product categories where most manufacturers and retailers are vertically integrated are cosmetics and healthcare products.

As a result of the changes on level of vertical integration of manufactures, in the last 10 years, many retailers have found themselves competing against their own suppliers.

¹²² Proportions are calculated out of all respondents to the retailer questionnaire active in the relevant product categories.

Vertical integration can have a positive impact on customers by virtue of streamlining the incentives of the manufacturing and the retail level.

3.4 Distribution via independent retailers

3.4.1 Introduction

(175) The preliminary results of the sector inquiry indicate that a wide variety of distribution agreements are used. These range from general terms and conditions of sale or general framework agreements without any selection criteria (with simple purchase order forms and confirmations) to territorial exclusive distribution, selective distribution and franchising agreements. In some limited instances, agency agreements are also used.

(176) In line with the focus of the sector inquiry being on contractual restrictions to e-commerce, this section reports on trends with regard to territorial exclusive distribution, selective distribution, and agency agreements, where the preliminary results of the sector inquiry show that restrictions on online sales are most prevalent.

3.4.2 Territorial exclusive distribution agreements

(177) In a territorial exclusive distribution agreement, the manufacturer agrees to sell its products only to one distributor (wholesaler or retailer) for resale in a particular territory.¹²³ While territorial exclusivity may reduce intra-brand competition and lead to market partitioning, it may also create efficiencies which justify certain territorial protection. The exclusive distributor may be incentivised to invest in additional promotion and marketing efforts, for example to introduce a product or brand in a new geographic market, on which other distributors could free ride absent any territorial protection.

(178) Territorial exclusivity is normally not granted for a specific sales channel (meaning offline or online), but in relation to all distribution activities in a certain territory. It therefore concerns both online and offline distribution activities. Given the potential of e-commerce for increased cross-border sales and the territorial restrictions inherent in territorial exclusivity, territorial exclusive distribution relationships and the underlying reasons for territorial exclusivity are analysed below in more detail.

(179) Exclusive territorial distribution agreements are exempted by the Vertical Block Exemption Regulation if the manufacturer's and the distributor's market shares do not exceed 30 % and provided that none of the hardcore restrictions listed in Article 4 of the Vertical Block Exemption Regulation are present.¹²⁴

¹²³ Exclusivity may also be granted in relation to certain customer groups. This Preliminary Report focuses in particular on cross-border sales and related restrictions and will therefore not examine exclusivity in relation to exclusively allocated customer groups. Moreover, based on the distribution agreements received the allocation of specific customer groups appears to be less widespread than the allocation of exclusive territories.

¹²⁴ Based on Article 4(b)(i) of the Vertical Block Exemption Regulation restrictions of the territory into which the buyer party to the agreement may sell the contract goods constitute a hardcore restriction, except where the

(180) The Commission questioned manufacturers as well as retailers about their usage of territorial exclusive distribution agreements in order to better understand the prevalence of territorial exclusive distribution and the reasons for its use.

3.4.2.1 Prevalence of territorial exclusive distribution

(181) Half of the manufacturers (49 %) that responded to the relevant question indicated that they make use of territorial exclusive distribution agreements.¹²⁵ However, the information received on distribution relationships between manufacturers and retailers shows that only a small portion of the relationships is based on territorial exclusivity, meaning that many respondents use territorial exclusivity in a limited number of their distribution contracts.¹²⁶

(182) Manufacturers provided information in relation to the territories within the EU in which they grant territorial exclusivity. Based on their responses, in some Member States territorial exclusivity is used more frequently, such as in Greece, Spain and Cyprus. Member States in which territorial exclusivity is less frequently used include for example Germany, Austria and Ireland.

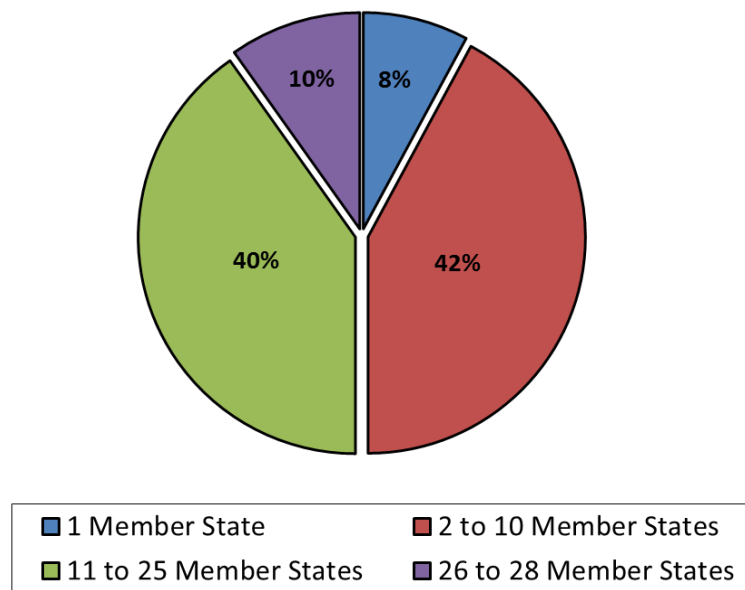
(183) As can be seen from Figure B. 26, 8 % of the manufacturers that provided this type of information use territorial exclusivity in one Member State only and most manufacturers use territorial exclusivity in multiple Member States. Territorial exclusivity is mostly granted in relation to entire Member States, but in some cases also in relation to certain regions, islands, cities or even airports.

restriction is limited to active sales into an exclusive territory reserved to the supplier or allocated to another distributor.

¹²⁵ Proportions are calculated out of 247 manufacturers that responded to the relevant question.

¹²⁶ One benefit of having an exclusive distributor for a certain territory is that a manufacturer does not need to have contractual relationships with multiple distributors. The fact that a single territorial exclusive agreement can cover an entire territory which would otherwise require multiple agreements can explain the low proportion of agreements that grant territorial exclusivity out of all agreements which manufacturers have in place.

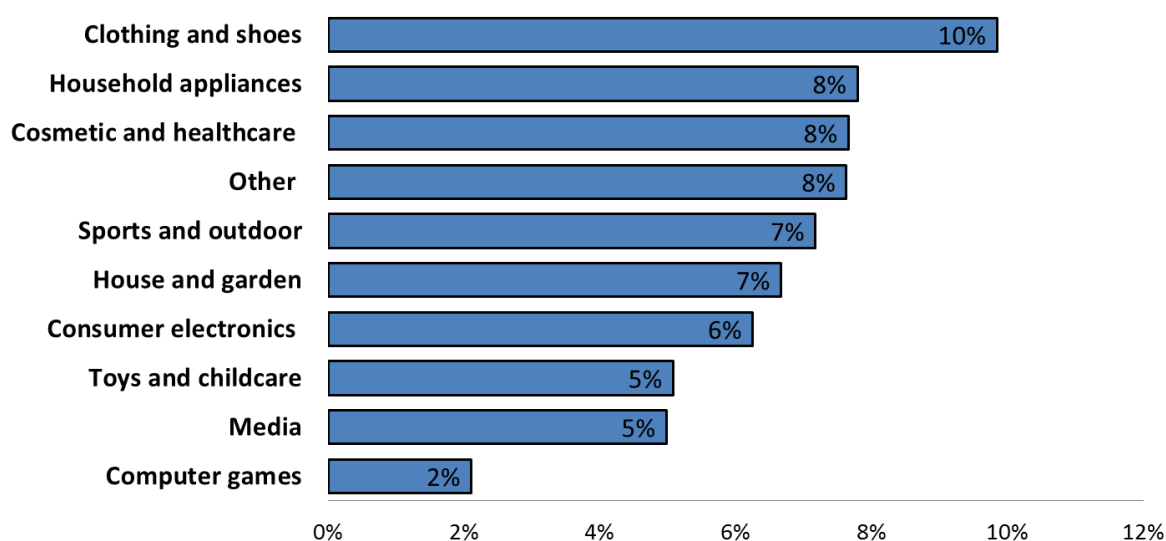
Figure B. 26: Proportion of manufacturers using territorial exclusive distribution agreements split by geographic coverage



(184) The Commission also asked retailers whether they act (in relation to some products) as an exclusive distributor for certain manufacturers. 11 % of respondents indicate that they concluded exclusive territorial distribution agreements with at least one manufacturer. The product category with the highest proportion¹²⁷ of retailers that have at least one territorial exclusive distribution agreement is clothing and shoes (10 %) followed by household appliances (8 %) and cosmetics and healthcare (8 %). A smaller proportion of respondents use exclusive territorial distribution agreements in the product categories media (5 %) and computer games and software (2 %).

¹²⁷ Proportions are calculated out of the total number of respondents active in each product category. A single respondent can be active in several product categories.

Figure B. 27: Use of exclusive territorial distribution agreements by retailers per product category



- (185) Manufacturers that make use of exclusive territorial distribution typically appoint an exclusive distributor at the wholesale level rather than at the retail level. They do so in particular in those Member States or territories where they do not have their own subsidiaries with a dedicated sales force. This may, for example, be typically the case in Member States considered to be too small in terms of business volume or where the brand is not sufficiently known to justify the setting up of a subsidiary. In such cases, manufacturers need experienced distribution partners with knowledge of local market conditions and who can reach out to retailers and undertake the investments necessary for launching, promoting and advertising a certain brand or product.
- (186) Exclusive distributors may also be useful in larger Member States where market structures are regionally fragmented and where customers typically buy from smaller or medium sized retailers rather than from a few large retail chains.
- (187) In some cases, territorial exclusivity at the wholesale level is combined with the operation of a network of authorized retailers with selective distribution at the retail level. In such a case, the exclusive wholesaler is in charge of developing and managing a network of authorised retailers according to the criteria defined by the manufacturer in a given Member State.
- (188) The development of this type of network may require significant investments by the wholesaler (e.g. for selection of and assistance to authorized retailers, promotion of the brand, control of the "closed" network, and application of the selection criteria in order to ensure high quality distribution and a consistent marketing strategy respecting the brand image).
- (189) Territorial exclusivity at the wholesale level is not necessarily linked with territorial (active) sales restrictions imposed on the exclusive distributor or on distributors in other

Member States or territories.¹²⁸ The manufacturer may simply decide to sell its products only via a single appointed wholesaler in a certain Member State or region. In such a case territorial exclusivity is limited to an obligation of the manufacturer not to appoint other wholesalers in the territory without granting the exclusive distributor any protection from sales coming from outside its territory.

3.4.2.2 Reasons for using territorial exclusive distribution agreements

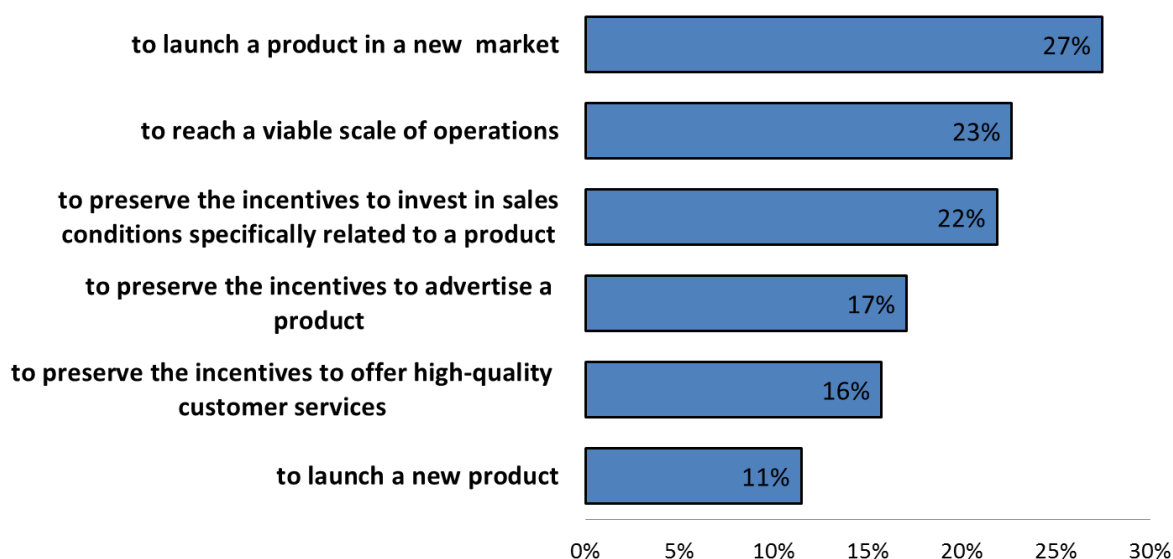
(190) Manufacturers were asked whether they consider granting territorial exclusivity to an independent distributor as necessary for a number of pre-defined reasons.

(191) As can be seen in Figure B. 28 below, granting territorial exclusivity was in particular considered as necessary in order to launch and establish a brand/product in a new (national) market. On average 27 % of the respondents in a product category consider it as necessary for this purpose. There is, however, significant variation across product categories. For instance, only 15 % of manufacturers active in consumer electronics consider exclusivity necessary to enter a new market as opposed to 46 % of respondents active in cosmetics and healthcare and 40 % active in sports and outdoor equipment.

(192) The second most mentioned reason for territorial exclusivity is in order to expand sales and reach a viable scale of operations (23 %) followed by the need to preserve the incentives of independent distributors to invest in facilities and human resources specifically related to selling the manufacturer's products (22 %). Manufacturers consider territorial exclusivity less relevant for launching and establishing a new brand/product (11 %) in an already served (national) market.

¹²⁸ For more details in relation to contractual territorial restrictions, see section B.4.3 Cross-border e-commerce and geographic restrictions to sell and advertise online on geographic sales restrictions.

Figure B. 28: Average proportion of manufacturers across product categories that consider granting territorial exclusivity necessary for each of the reasons mentioned¹²⁹



(193) The responses of the manufacturers show that granting territorial exclusivity to distributors is normally not a general distribution policy applied by the manufacturer across all Member States and brands/products concerned. It is rather a case-by-case decision for which the manufacturer takes into account the product and brand characteristics, the local market conditions (size, maturity and structure of the market) as well as its knowledge of the market.

(194) Whether territorial exclusivity is granted depends also on the willingness of distributors to enter into a distribution agreement absent any territorial exclusivity. In some markets (e.g. decorative cosmetics) territorial exclusivity has been reported to be a standing industry practice. In these markets distributors will typically not be prepared to enter into a distribution arrangement without territorial exclusivity.

(195) Exclusivity may be considered necessary by manufacturers (and demanded by distributors) to protect against free-riding from other distributors in cases in which a distributor is required to significantly invest in order to build up a business in a certain territory. Such investments can among others relate to necessary warehouse facilities and the setting up of logistical distribution arrangements; human resources such as sales and back-office personnel; showrooms; high-quality customer services; and promotion and marketing activities. Territorial exclusivity can guarantee a sufficient return on investment for the distributor and thereby ensure a long-term commitment. Without

¹²⁹ The percentages for each of the listed reasons are calculated as the weighted average of the proportions of respondents in each product category, out of all respondents in this product category, who consider territorial exclusivity necessary for that particular reason. The weights reflect the distribution of respondents to the questionnaire across product categories.

territorial exclusivity distributors may in certain cases not be willing to enter into a distribution agreement and commit to these investments.¹³⁰

(196) Territorial exclusivity may also be useful for a number of other reasons not mentioned in the above figure. Dealing with only one distributor in a certain Member State is considered by some manufacturers as beneficial as it allows for efficiently monitoring the performance of the distributor and coordinating both parties' promotional and presentational efforts in order to communicate a consistent brand image. Having a single distributor also simplifies business processes (e.g. fewer agreements to negotiate and fewer orders to execute) thereby reducing transaction costs.

(197) Retailers were also asked whether they consider territorial exclusivity as a necessary or very important factor for a number of pre-defined reasons.¹³¹ Most retailers do not consider territorial exclusivity as necessary or important. Out of the 673 retailers that responded to this question 82 % do not consider territorial exclusivity as a necessary or important factor for any of the reasons provided. For those that consider territorial exclusivity as a necessary or important factor, the reasons for which territorial exclusivity is mostly considered as relevant are entering a new market, launching a new product/brand or expanding and reaching a viable scale of operations. Retailers consider territorial exclusive distribution less important for incentivising them in investing in advertising and promotion of certain brands or products. However, as indicated earlier, exclusivity is more widespread on wholesale than on retail level.

Summary

Almost half of the respondent manufacturers make use of territorial exclusive distribution agreements. However, in terms of numbers, only a small portion of their distribution relationships is actually based on territorial exclusivity.

Whether to use exclusive territorial distribution is typically decided by manufacturers on a case-by-case basis, taking into account product and brand characteristics, local market conditions as well as the own knowledge of the market.

Manufacturers that make use of territorial exclusive distribution typically appoint an exclusive distributor at the wholesale level rather than at the retail level. In some cases, territorial exclusivity at the wholesale level is combined with the operation of a network of authorized retailers within a selective distribution network. In this case, the exclusive wholesale distributor is in charge of developing and managing a network of authorised retailers according to the criteria defined by the manufacturer in a given Member State.

Granting territorial exclusivity is in particular considered as necessary in order to launch and establish a brand/product in a new (national) market. Almost one-third of the respondent

¹³⁰ This may be even more so, if the distributor is required to set-up mono-brand stores in which only the manufacturer's products are sold.

¹³¹ These reasons were: expanding and reaching a viable scale of operations, entering a new market, launching a new brand/product and investing in advertising and promotion of certain brands or products.

manufacturers in a given product category consider it as necessary for this purpose. There is, however, significant variation across product categories.

Exclusivity is also considered necessary (and demanded by distributors) to protect against free-riding by other distributors in cases in which a distributor is required to significantly invest in order to build a business in the exclusively allocated territory.

3.4.3 Selective distribution

3.4.3.1 Overview and development of selective distribution

(198) In selective distribution systems, distributors are selected on the basis of specific criteria, set out in the distribution agreement.

(199) Changes to the selective distribution systems represent one of the most frequent reactions of manufacturers over the last 10 years to the growth of e-commerce. Most manufacturers (56 %) that responded to the relevant question indicate that they make use of selective distribution agreements for some of their products.¹³²

(200) When asked about the measures they took in reaction to the growth of e-commerce in the last 10 years, 19 % of manufacturers report having introduced a selective distribution system where they did not apply selective distribution beforehand, while 2 % extended their existing selective distribution systems¹³³ to other types of products. 67 % of manufacturers that use selective distribution¹³⁴ report having introduced new criteria in their distribution agreements.

(201) The adaptation of the selection criteria to online (pure online or hybrid) retailers is reported widely. A frequent way of introducing such changes is the creation of an "internet addendum" to the existing distribution agreements that sets out the selection criteria for online distribution.

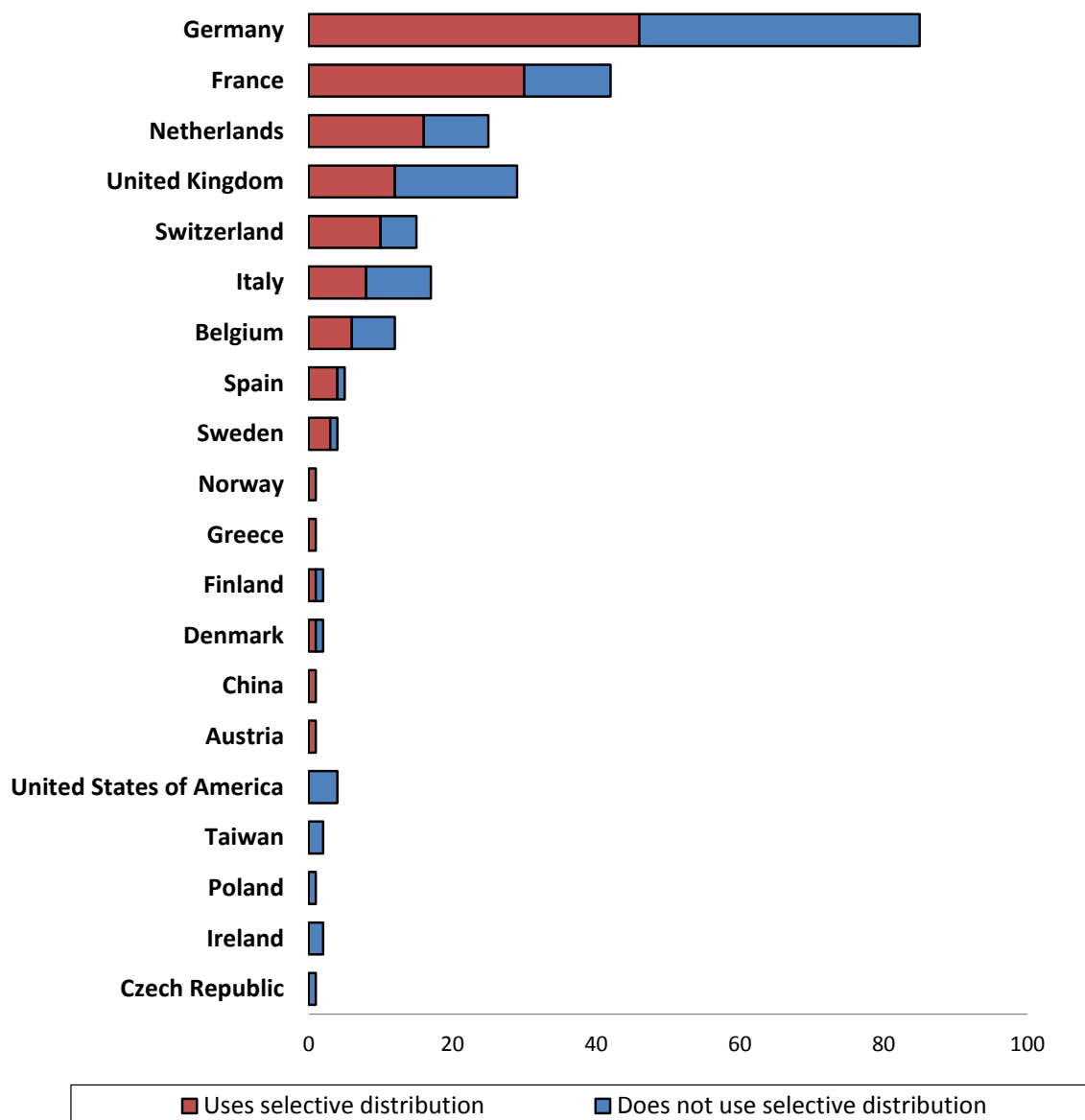
(202) Figure B. 29 below shows the use of selective distribution, by reference to the number of manufacturers that responded to the relevant question, by Member State of origin of the respondent manufacturer. Slightly more than half of German respondent manufacturers use selective distribution, while this share is significantly higher in France, and lower in the United Kingdom.

¹³² Proportions calculated out of 252 manufacturers that responded to the relevant question.

¹³³ Proportions calculated out of 244 manufacturers that responded to the relevant question.

¹³⁴ Proportion calculated out of 141 manufacturers that reported they were using selective distribution. This ratio corresponds to 39 % of all 244 manufacturers that responded to the relevant question, including those that do not use selective distribution.

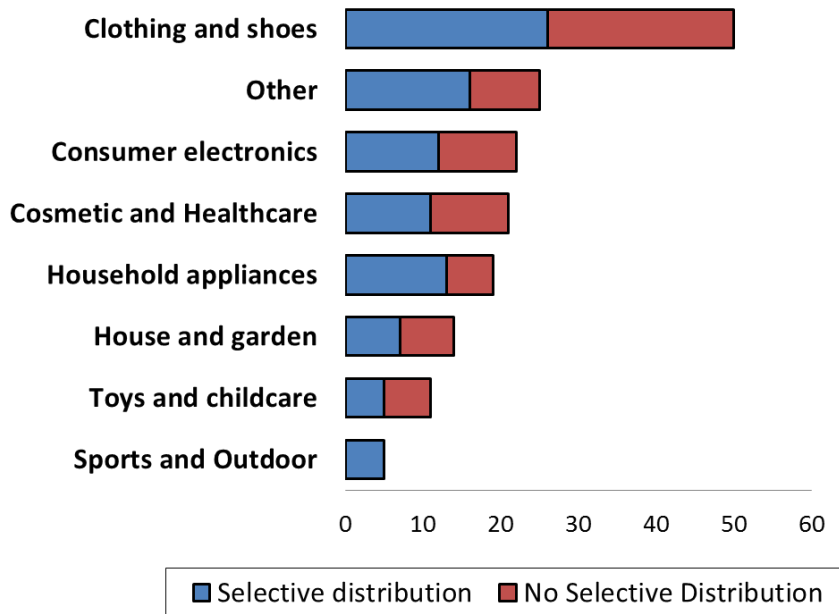
Figure B. 29: The use of selective distribution, by Member State of origin of respondent manufacturers (number of manufacturers)¹³⁵



(203) Figure B. 30 below provides an indication of the share of manufacturers per product category (covered by the sector inquiry) that make use of selective distribution.

¹³⁵ Based on the responses by 252 manufacturers.

Figure B. 30: Number of respondent manufacturers that are active in one product category only and sell via selective distribution or other forms of distribution¹³⁶

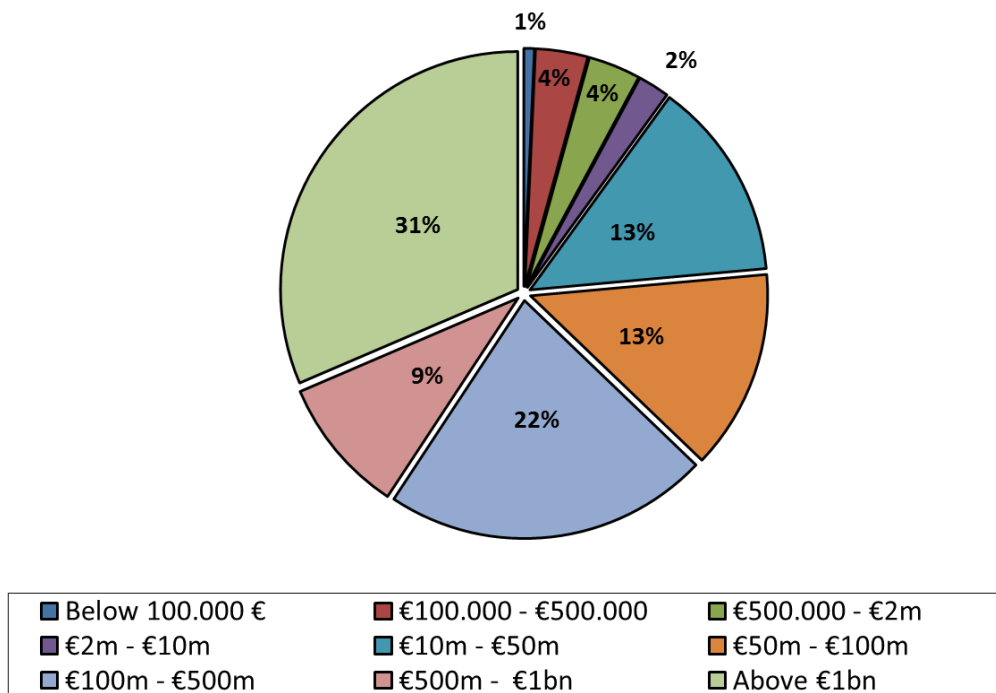


(204) Selective distribution thus is used by more than half of the manufacturers in the product categories of clothing and shoes, cosmetics and healthcare, consumer electronics and household appliances, but also fairly widespread in the other product categories.

(205) The following Figure B. 31 shows the distribution of manufacturers using selective distribution, by turnover. Almost one third of manufacturers using selective distribution has a turnover over EUR 1 billion, and almost two third over EUR 100 million.

¹³⁶ For the purpose of this figure, only the manufacturers active in one product category were taken into consideration.

Figure B. 31: Manufacturers using selective distribution, by turnover in 2014¹³⁷

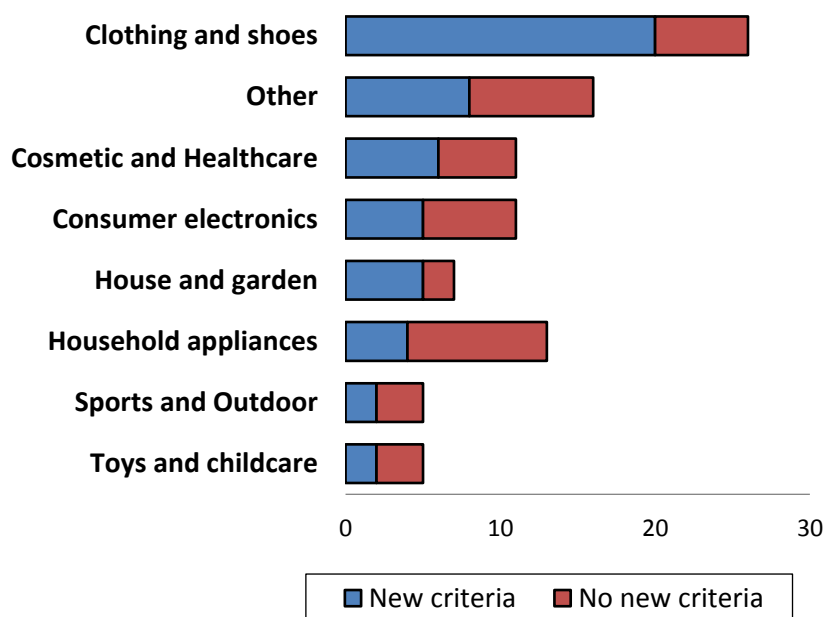


(206) As mentioned above, 67 % of manufacturers that use selective distribution¹³⁸ report having introduced new criteria in their distribution agreements in the last 10 years. This share is even higher in the categories of clothing and shoes (77 %), and house and garden (71 %). Figure B. 32 shows the number of manufacturers that were already using selective distribution and introduced new selection criteria in the last 10 years, per product categories.

¹³⁷ Based on the responses of 141 manufacturers that use selective distribution.

¹³⁸ Proportions are calculated out of 141 manufacturers that use selective distribution. This ratio corresponds to 39 % of all 244 manufacturers that responded to the relevant question, including those that do not use selective distribution.

Figure B. 32: Number of respondent manufacturers that sell via selective distribution and introduced new selection criteria in the last 10 years¹³⁹



3.4.3.2 The reasons for opting for selective distribution

(207) For the purpose of providing a comprehensive overview of the typical selection criteria applied in selective distribution agreements across the different product categories covered by this Preliminary Report, as well as of the reasons leading to the above mentioned changes and their impact on retailers, both manufacturers and retailers were asked a number of questions relating to selective distribution.

(208) Manufacturers were asked to describe their main reasons for operating a selective distribution system and for the application of the criteria set out in their selective distribution agreements.

(209) In general, manufacturers stress the importance of high quality distribution as an important factor of competition, affecting brand image, the quality of pre- and after-sales services and the overall "shopping experience" of customers. The most typical reasons put forward for operating a selective distribution system are set out below:¹⁴⁰

- (a) to protect market positioning;
- (b) to preserve brand image / reputation;
- (c) to ensure an environment for the sales point that mirrors the brand's market positioning and reputation;

¹³⁹ For the purpose of this figure, only the manufacturers active in one product category, and using selective distribution in that product category, were taken into consideration.

¹⁴⁰ Based on the responses by 165 manufacturers.

- (d) to preserve the prestige and luxury perception and reputation of the products / brand;
- (e) to respond to customer expectations when buying premium brands / premium products of brands;
- (f) to ensure high quality pre- and after-sales services with skilled, professional staff, able to provide quality/professional advice (also, in the case of certain products, with a view to ensuring safe use of the product);
- (g) to ensure individualised advice to customers / to best respond to individual needs and follow-up / to achieve customer engagement;
- (h) to ensure the highest quality of technical presentation by specialists / highest level of information about product, about compatibilities with other products, about installation;
- (i) to ensure a coherent and homogenous presentation of the products within the EU, with a view to conveying a coherent "message" to customers. This includes design and esthetical coherence of product presentation;
- (j) to guarantee an overall positive shopping experience to customers;
- (k) to avoid or minimise free-riding by online sales channels on investments by high-quality physical points of sale;
- (l) to protect products more efficiently against counterfeit products by increased traceability.

(210) The reasons put forward by the manufacturers do not vary considerably depending on the product categories: the above justifications are equally put forward by manufacturers of clothing and shoes, of electronic devices, of toys, cosmetics or of sports equipment.

(211) To provide a few examples, in addition to the clothing, cosmetics and consumer electronics sectors, where selective distribution is wide-spread, selective distribution systems are largely used by manufacturers of kitchen appliances, gardening equipment, cleaning equipment, sports shoes and sports accessories, toys, prams and other accessories for babies, accessories and food for animals (pets), hair-dryers and other hair-care equipment or trekking equipment.

(212) Several brand owners report about a differentiated distribution system, whereby only the premium product line is sold under selective distribution, while the rest of their products are sold in open distribution.

(213) Other manufacturers report about multi-level selective distribution systems, where most of the authorised retailers only get access to a certain part of the entire product range. The more additional selection criteria a retailer fulfils, the bigger the part of the product

range he or she can distribute. In these multi-level selective distribution systems, the different levels of selected retailers are contractually restricted from selling a given product (line) to those retailers that are not authorised to sell that product (line): i.e. to those retailers that are at a lower level in the selective distribution system.

(214) The idea behind these multi-level systems is usually to differentiate between the "mass-distribution" of a wide range of products with a lower threshold of quality requirements and the high-quality distribution of the premium or high-end product lines, with a high threshold of qualitative criteria. As a result, while not all authorised retailers of the same brand necessarily comply with the same set of criteria¹⁴¹, those that sell the same product range do so.

3.4.3.3 *The selection criteria*

(215) Both manufacturers and retailers were asked to describe the criteria listed in their selective distribution agreements. In addition, manufacturers were asked to provide for each of the Member States with the highest sales in 2014, the selective distribution agreements with the three largest independent distributors. Many of the submitted agreements by retailers, in response to other questions, are also selective distribution agreements.

(216) Based on the above information, the most typical examples of criteria applied (a) to both online and offline sales, (b) specifically to offline sales, and (c) specifically to online sales, are set out below¹⁴²:

- (a) Typical examples of selection criteria in relation to both online and offline sales:
- promotional / marketing campaigns must be pre-approved by brand/ must adhere to brand's promotion policy;
 - marketing material must be pre-approved by brand;
 - respect of fixed criteria relating to marketing campaigns;
 - marketing must be targeted to certain territories;
 - ensure shipment and installation service / ensure shipment and installation service within a given number of hours / days;
 - fulfil criteria for quality and rapidity of repair / after-sales services;
 - have at least one physical point of sale / showroom;
 - respect determined volume restriction per order;

¹⁴¹ Certain retailers may have to fulfil more criteria than others but get access to a broader / the full range of products of the brand.

¹⁴² Based on the responses of 178 manufacturers and 169 retailers.

- keep appropriate level and immediate availability of stock;
- offer an appropriate / representative level of product range out of the brand's products;
- respect minimum purchase quantity;
- dispose of a minimum annual turnover per point of sale;
- point of sale must be specialised in the sale of the given category of products (for instance, specialised in gardening / kitchen appliances / lightening);
- products of the brand must represent a certain fixed minimum/maximum share of all products sold in the point of sale;
- no sale of other products that may harm the image of the brand;
- respect specific criteria for presentation of new product lines;
- not to remove or alter serial numbers;
- send regular sales reports to the manufacturer;
- comply with storing and shipment conformity rules (such as safe packaging, respecting temperature / humidity / other storage conditions).

(b) Typical examples of specific criteria in relation to offline sales:

- geographic location criteria (for instance in city centre / high street / premium shopping mall / walking area / easy access / ensuring parking area / immediate neighbourhood of shop must reflect similar standing);
- minimum number of sales points in a given geographic area;
- minimum size of the physical shop;
- quality requirements for inside aspect of the shop (for instance with respect to fixtures, furnishing, design, lightening, floor coverings);
- product presentation requirements (such as the minimum number of colour options displayed next to each other, a minimum number of the brand's products exposed, the minimum space requirement between products/product lines /brands in the shop);
- minimum number of competing brands (of same product category and of similar quality) exposed near to brand;

- minimum number of staff present in shop;
- trained staff and/or training requirements for staff;
- dedicated, distinct area for the brand in the shop ("shop in the shop");
- ban of resale via outlets;
- minimum space (m² / number and size of shelves, etc.) reserved for the brand;
- specific, distinct area for demonstration of products / personnel able to provide technical presentation of all qualities of product and advise on technical aspects;
- ways to ensure that customers can directly try the product (for instance availability of fitting rooms)/ in case of audio-visual presentation: with latest digital content provided by brand, such as TV demonstration, music);
- minimum opening hours;
- minimum number of cash registers corresponding to shop's size;
- quality of gift-wrapping; and
- quality appearance of staff.

(c) Typical examples of specific criteria in relation to online sales:

- the retailer must own the website / operate the website directly;
- the website must be pre-approved by the manufacturer;
- discount websites or websites perceived as discount websites are excluded;
- different criteria relating to the "high-end" look and feel of the website;
- for product presentation (product description, agreed videos, pictures) and website design, display only of pre-approved content (images/text) / of content fully prepared by manufacturer;
- prohibition to sell the products via all or certain third party platforms (marketplaces);
- in case of launch of a new website, the website must be pre-approved by the manufacturer;

- prohibition to promote via third party websites (such as price comparison tools);
- requirements relating to the search criteria applied by website to identify a product;
- set of criteria aiming at a clear and easy navigation on the website;
- criteria for the domain name of website (such as the domain name must correspond to the name of the authorised retailer / domain name of website and name of the brick and mortar shop of the retailer must correspond / must suit the brand image);
- the website should be specialised in sale of products of the same product category;
- criteria relating to the display of the product on the website, (such as the requirement to display the brand's products only amongst products with similar quality reputation, 360° videos, picture quality, not to display products next to unrelated product categories, products of the brand displayed as a "block", i.e. not mixed with other brands);
- requirement to display the agreed logo (typically logo of the brand or logo of the authorised retailer or text identifying the brand or the authorised retailers, such as "authorised ____ (brand) partner");
- website's general conformity with brands' graphical and picture identity, quality and standards / compliance with graphic charter of the brand;
- prohibition of using links, messages, banners or any images that may negatively affect brand reputation;
- banning links to any other website;
- criteria relating to banners / banners must direct customers to official brand website / to physical shops;
- banning pop-up windows;
- offering the option to the customer to create an account;
- requiring immediate notification of counterfeit products / removal of counterfeit products within a limited number of hours;
- requiring the use of secure payment systems;
- respecting detailed criteria for online product marketing;

- option to have a separate webpage / dedicated brand area (online "shop in the shop");
- technical requirements for the website, such as fixed % of availability of website (99.9 % availability rate...) or rapidity of website;
- option to "like" products on Facebook and follow the Tweets by the brand;
- providing product descriptions that notify customers if a newer version of the product is available;
- displaying accessories of products;
- prices displayed inclusive of shipping costs;
- responding to online enquiries of customers within a given number of hours/days;
- providing call centre / hotline or other personal availability for support via phone (including quality criteria for the hotline, such as rapidity of answering calls, professionalism, availability hours);
- clearly displaying delivery terms and conditions and providing information to customer on delivery date;
- organise warranty / repair / after-sales services of products;
- displaying available stock;
- maintaining a representative line of products on the website;
- sending confirmation of orders by individual e-mail;
- banning advertising banners on of product presentation pages;
- criteria for search key-words (that must be compatible with brand image);
- introducing a procedure to certify customer reviews to make sure they reflect of views of real buyers;
- displaying a FAQ page;
- website must be hosted by a reputable service provider / reliable server / sufficient bandwidth;
- free trial option for customers;
- requirements relating to the language versions of the website.

- (217) In many cases, the criteria introduced for online sales mirror the quality requirements for offline sales. The often detailed online sales requirements reflect a clear intention by the manufacturers to keep control of the environment where the product is presented, the coherent brand-marketing of the product and the quality of the display of the product itself.
- (218) To get a better overview of the tangible impact of the introduction of selective distribution criteria for online sales, retailers were asked whether they have been removed from a selective distribution network in the last three years as a result of a change in the criteria required by the supplier for online selling. Out of 904 responses, 108 retailers (12 %) responded that they had indeed been removed from a selective distribution network in the last three years as a result of the new criteria for online sales.
- (219) Retailers were also asked whether any supplier refused their admission to a selective distribution network in the last three years because they were selling online or because of the way or geographic area where they were selling online. Out of 901 responses, 173 (19 %) confirmed that their admission to a selective distribution network had been refused by at least one supplier, for the above reasons, in the last three years.

3.4.3.4 Pure online players in selective distribution

- (220) Overall, a large majority of the manufacturers using selective distribution¹⁴³ exclude pure online players from their selective distribution network for at least part of their products. 47 % of the manufacturers using selective distribution¹⁴⁴ reported that they do not accept pure online players to their selective distribution network, while many of the remaining manufacturers reported that they accepted pure online players for the distribution of part of their products, but required the presence of at least one brick and mortar shop for their high-end/ professional/ latest product lines.
- (221) The need to ensure proper advice to customers by qualified staff; the possibility to demonstrate the operation/ the use/ technical specificities of the product; the ability of customers to visualise the product; the luxury environment when presenting the product; special shopping experience, with personalised care and attention; and safety demonstration and explanations are the main reasons listed by the manufacturers for requiring their distributors to operate at least one brick and mortar shop.
- (222) While many of the criteria applied for brick and mortar distribution can be mirrored by equivalent requirements for online distribution, the above mentioned requirements are claimed by some manufacturers to be inherently linked to brick and mortar distribution, impossible by nature to be reproduced in an equivalent manner and with equivalent results for customers, in a purely online environment. On the other hand, a number of retailers expressed concerns regarding the requirement of having a brick and mortar

¹⁴³ Based on the responses of 166 manufacturers to this question.

¹⁴⁴ Based on the responses of 166 manufacturers to this question.

shop which, in their view, would not be justified by the nature of the products and would not correspond to the actual needs of customers in relation to those products.

3.4.3.5 General considerations on selective distribution

- (223) The preliminary findings of the sector inquiry suggest that the use of selective distribution systems has significantly increased with the growth of e-commerce.
- (224) The Commission recalls that according to established case-law the organisation of a selective distribution network is not prohibited by Article 101(1) TFEU, to the extent that resellers are chosen on the basis of objective criteria of a qualitative nature, laid down uniformly for all potential resellers and not applied in a discriminatory manner, that the characteristics of the product in question necessitate such a network in order to preserve its quality and ensure its proper use and, finally, that the criteria laid down do not go beyond what is necessary.¹⁴⁵
- (225) Qualitative and quantitative selective distribution agreements are exempted by the Vertical Block Exemption Regulation as long as the market share of both supplier and buyer each do not exceed 30 %. The Vertical Block Exemption Regulation exempts selective distribution regardless of the nature of the product concerned and regardless of the nature of the selection criteria as long as none of the hardcore restrictions listed in Article 4 are present. However, where the characteristics of the product do not require selective distribution or do not require the applied criteria, such as for instance the requirement for distributors to have one or more brick and mortar shops or to provide specific services, such a distribution system may not generally bring about sufficient efficiency enhancing effects to counterbalance a significant reduction in intra-brand competition. Where appreciable anti-competitive effects occur, the benefit of the Block Exemption Regulation is likely to be withdrawn.¹⁴⁶
- (226) The preliminary findings of the sector inquiry lead to the following general observations in this regard.
- (227) First, the number and variety of products for which selective distribution is being applied has increased considerably.
- (228) Second, based on the information available to the Commission as a result of the sector inquiry, the use of certain clauses in selective distribution agreements, depending on the products for which they are used, may require closer scrutiny. For example, the requirement for retailers to operate at least one brick and mortar shop (thereby excluding all pure players from selective distribution), while generally covered by the

¹⁴⁵ Judgment in *Metro SB-Großmärkte v Commission*, 26/76, EU:C:1977:167, paragraph 20, judgment in *L'Oréal*, 31/80, EU:C:1980:289, paragraphs 15 and 16, judgment in *Allgemeine Elektrizitäts-Gesellschaft AEG-Telefunken*, 107/82, EU:C:1983:293, paragraph 35, judgment in *Groupement d'achat Edouard Leclerc*, T-19/92, EU:T:1996:190, paragraphs 112 to 120 and judgment in *Pierre Fabre Dermo-Cosmétique SAS*, C-439/09, EU:C:2011:649, paragraph 41.

¹⁴⁶ See paragraph 176 of the Vertical Guidelines.

Vertical Block Exemption Regulation, may need further assessment in individual cases when used for certain product categories or certain lines of products which pure online retailers might be equally qualified to sell.¹⁴⁷

(229) Third, several retailers complained about the lack of transparency and objectivity of the selection criteria used by the manufacturers to choose the members of their distribution network.

(230) In particular a number of retailers that qualify themselves as "discount" retailers raised concerns. These retailers suggest that even if they complied with all quality criteria, the suppliers would refuse their admission to the network due to the low retail prices they set for the products. Due to high price transparency online, these retailers would be seen by manufacturers as driving product prices down, thereby putting at risk the margins of many other authorised retailers in the distribution network.

(231) When asked about the transparency of their selection criteria, 24 % of the manufacturers¹⁴⁸ report that they do not communicate their selective distribution criteria to retailers wishing to be part of their selective distribution network. Out of the 76 % that communicate their selection criteria to retailers, some however specify that they would not necessarily do so when, based on information available to them regarding the retailer (such as for instance the lack of a brick and mortar shop), it clearly appears that the retailer would anyway not fulfil their set of selection criteria. These manufacturers typically explain that they would however send a letter to the retailer setting out the reason for the refusal.

(232) In light of these observations, the Commission may investigate possible anti-competitive clauses in selective distribution agreements restricting online sales.

Summary

Increased recourse to selective distribution as well as the use of new selection criteria represent one of the most frequent reactions of manufacturers over the last 10 years to the growth of e-commerce. 56 % of manufacturers that responded to the relevant question indicate that they make use of selective distribution agreements.

The sector inquiry shows a more widespread use of selective distribution by manufacturers with relatively higher annual turnovers: one third of manufacturers using selective distribution have a turnover over EUR 1 billion, and almost two third over 100 million.

Selection criteria in selective distribution agreements vary significantly depending on the sales channel (online/offline). Manufacturers reason the requirements to a large extent by the need to ensure high quality distribution, coherent brand image and the quality of pre- and

¹⁴⁷ See paragraph 176 of the Vertical Guidelines.

¹⁴⁸ Based on 171 responses to this question.

after-sales services, with a view to guaranteeing an overall high quality "shopping experience" for customers.

However, the use of certain clauses restricting online sales in selective distribution agreements, depending on the products for which they are used, may go beyond what is necessary. As an example, a large majority of the manufacturers using selective distribution exclude pure online players from their selective distribution network for at least part of their products. The requirement for retailers to operate at least one brick and mortar shop, which is generally block exempted, may, in some cases, go beyond what is necessary for the purpose of ensuring high quality distribution.

In addition, several retailers complained about the lack of transparency and objectivity of the selection criteria used by the suppliers to choose the members of their distribution network.

The Commission may investigate possible anti-competitive clauses restricting online sales in selective distribution agreements.

3.4.4 Agency agreements

(233) An agent is a legal or physical person vested with the power to negotiate and/or conclude contracts on behalf of another person (the principal), either in the agent's own name or in the name of the principal, for the sales of the goods/services of the principal.¹⁴⁹ The typical agent/principal relationship in retail markets, such as those covered by the sector inquiry, are the ones where retailers act as agent selling goods on behalf of manufactures. The manufacturers involved in the sector inquiry reported using agency agreements rather exceptionally.

(234) Approximately 19 % of manufacturers indicate using this type of agreement in at least one contractual relationship.¹⁵⁰ The majority of them report, however, that those agreements constitute a rather small percentage of their distribution relationships (single digit percentages, and in some cases below 1 %) and do not represent a significant proportion of their total turnover. In many cases, sales via agents amount to less than 1 % of the total turnover of the manufacturer.

(235) Agency agreements are most commonly used by manufacturers active in the clothing and shoes sector. There are no significant differences as regards the use of agents by manufacturers in different Member State.

(236) Manufacturers use agency agreements for a variety of purposes but the rationale is mostly the same namely to exercise more control over the distribution of their products, especially in markets where the manufacturer does not have its own sales force.

¹⁴⁹ See paragraphs 12 et seq of the Vertical Guidelines. An agent can also purchase goods or services on behalf of the principal.

¹⁵⁰ Proportions are calculated out of all 259 manufacturers that replied to the questionnaire.

- (237) The use of agency agreements is seen by manufacturers as a way to exercise control with lower fixed costs. Many of the agency agreements provided by manufacturers contain detailed requirements on how the agent should carry out its activities and, often, on how the agent is to report extensively on market conditions, customers' feedback, and product performance.
- (238) Few manufacturers also use agents to provide more services and assistance to customers. Agents are in most cases equally used in online and offline channels, although it was occasionally reported by few manufacturers that they use agents only in one of these channels.
- (239) The agency agreements that manufacturers provided to the Commission in the course of the sector inquiry are almost exclusively with wholesalers. In those cases the agreements establish that the wholesaler is under the obligation to ensure that the retailers comply with established quality criteria for the sale of products. In many instances, the duration of the agency agreement is indefinite, either because the agreement provides for it, or the agreements are automatically renewed after a given duration.
- (240) Marketplaces can also act as agents of professional sellers. However, this type of relationship is not frequently used. Only 8 % of all of respondent marketplaces report that they do act as an agent for their sellers.¹⁵¹ The turnover achieved by marketplaces through this type of agreements is however not insignificant and, in certain cases, can reach almost EUR 200 million.
- (241) Entering into an agency relationship gives principals stronger control over the agent as compared to independent distributors. For instance, restrictions regarding prices or the geographic scope of the agent's sales activities are not caught by Article 101(1) TFEU when they occur within a genuine agency relationship.¹⁵²
- (242) This enhanced control comes at a cost. For the relationship to be considered genuine agency, it is essential that the agent does not bear any, or bears only insignificant financial or commercial risks in relation to the activities for which it is appointed.¹⁵³ Another element to take into consideration to establish whether or not an agent can be considered genuine is whether an agent acts on behalf of one or more principals.¹⁵⁴
- (243) Certain provisions concerning the relationship between the agent and the principal, such as single branding provisions or post-term non-compete, may, under certain

¹⁵¹ Proportions are calculated out all marketplaces (37) that replied to the questionnaire.

¹⁵² Judgment in *DaimlerChrysler v Commission*, T-325/01, U:T:2005:322, paragraph 122 and judgment in *Confederación Española de Empresarios de Estaciones de Servicio*, C-217/05, EU:C:2006:784, paragraph 62. See also Vertical Guidelines, paragraph 18.

¹⁵³ See Vertical Guidelines, paragraphs 12-17.

¹⁵⁴ Judgment in *Vereniging van Vlaamse Reisbureaus*, 311/85, EU:C:1987:418, paragraph 20.

circumstances, infringe Article 101(1) TFEU.¹⁵⁵ Those provisions may benefit from the Vertical Block Exemption Regulation, in particular if the conditions of Article 5 of that regulation are fulfilled.¹⁵⁶

Summary

Agency agreements are not commonly used in the product categories covered by the sector inquiry. Less than a fifth of the respondent manufacturers use this type of agreement while less than 1 in 10 marketplaces would act as an agent for their professional sellers. Manufacturers use agency agreements with their wholesalers rather than with retailers. They do so to exercise increased control over the distribution of their products while saving on the costs of setting up their own sales force/infrastructure in a given market.

Agency relationships allow for better control over retail activities than other distribution models, for instance over prices or the geographic scope of sales. However, this comes at a cost for the principal who must make sure that the agent does not bear, or only bears to a limited extent, any financial or commercial risks for its activities.

4. RESTRICTIONS TO SELL AND ADVERTISE ONLINE

4.1 Motivations for restrictions

(244) Manufacturers may employ different price and non-price restrictions (vertical restraints) in their agreements with retailers, with the aim of protecting their reputation for quality and brand image, limiting free-riding and incentivising retailers to provide demand enhancing customer services and promote their brands and products.

(245) On the other hand, increased online price transparency and the resulting enhanced price competition may also lead retailers to put pressure on manufacturers for ensuring a certain level of minimum resale prices throughout the distribution network, or a certain level of guaranteed profit margin.

(246) The sector inquiry provides insights into the prevalence and importance of these considerations. This section presents the preliminary findings regarding (i) the importance of, product quality, brand image and price, (ii) customer services offered at the retail level, as well as promotion and advertising and (iii) free-riding between the online and the offline retail channel. A more detailed presentation of the motivations behind specific vertical restraints is provided in the sections dedicated to the different types of restrictions.

¹⁵⁵ Exclusive agency provisions prevent the principal from appointing other agents in respect of a given type of transaction, customer or territory. Single branding provisions prevent the agent from acting as an agent or distributor of undertakings which compete with the principal. See also Vertical Guidelines, paragraph 19.

¹⁵⁶ See Vertical Guidelines, paragraph 19.

4.1.1 Product quality, brand image and price

- (247) The preliminary results of the sector inquiry (see section B.2.2) reveal that the great majority of manufacturers in all product categories consider the quality of the product and the brand image to be of high importance for their ability to attract customers. A much lower proportion of manufacturers considers the price to play a primary role to attract customers.
- (248) At the same time, among the different parameters of competition at the retail level, price is most often considered as important by retailers. Relatively fewer respondent retailers attach such a high level of importance to product quality.
- (249) The possibility of misaligned incentives when it comes to building and maintaining a brand image and quality reputation may lead manufacturers to seek to achieve this goal by means of contractual obligations in distribution agreements. For instance, as outlined in section B.3.4.3, manufacturers might find it necessary to introduce selective distribution systems for certain products or introduce detailed selection criteria.
- (250) Some manufacturers explain how sales on marketplaces could undermine the brand image, especially in the case of premium products. This is presented as an important consideration with regard to marketplace restrictions (see section B.4.4). Moreover, as outlined in more detail in section B.4.5, the main reasons for manufacturers' limiting the use of price comparison tools are the protection of the brand image and the quality standard of distribution.
- (251) Similarly, one of the reasons stated by manufacturers for recommending retail prices to retailers (see section B.4.6) is to signal the quality of their product and to create or convey a desired brand image. This is particularly relevant for premium products.

4.1.2 Customer services, promotion and advertising

- (252) In principle, customer services at the retail level can play a complementary role in conveying a certain brand and quality image, as well as in enhancing demand for a manufacturer's products. A comment by one respondent manufacturer captures this consideration: *"[...] a manufacturer of quality brands and products [...] strongly depends on the retail level for conveying the characteristics and features of its products, as well as their quality and image, to consumers. Accordingly, the efforts and investments made at the retail level, [...] are extremely important for enhancing the demand for the brands and products. The company wants dealers to present its products in an attractive way, to respect the corporate identity of its brands, and to provide to consumers all the information they need to take an informed purchasing decision."*
- (253) When it comes to value added customer services offered by retailers, the majority of respondent manufacturers (85 %) consider such services (in particular pre-sale services such as showroom presentation by dedicated staff, customer support, call centres) to be

important for enhancing demand for most or some of their brands/ products.¹⁵⁷ As explained in section A.4., selective and exclusive distribution, as well as certain price restraints may be partly motivated by manufacturers' willingness to incentivise retailers to provide more of these services.

- (254) The preliminary results of the sector inquiry show that 75 % of the manufacturers that consider customer services at retail level as important¹⁵⁸ sell their products via a selective and/or territorial exclusive distribution system,¹⁵⁹ while 85 % recommend sales prices to retailers or wholesalers. 66 % of the manufacturers that consider customer services at the retail level as important monitor the level and/or quality of these services.¹⁶⁰ Depending on the product, a considerable number of manufacturers also request retailers to have a brick and mortar shop or to invest in point-of-sale or shop-in-shop brand presentation.¹⁶¹
- (255) The preliminary findings of the sector inquiry show that the more the manufacturer participates financially in providing customer services, and the more stringent the obligations on retailers are, the more intensively manufacturers monitor the compliance and performance of the retailers. Thus, some only monitor regularly services for premium brands/models and carry out random checks for others; others regularly visit, audit, inspect and carry out shop satisfaction surveys and engage in mystery shopping. The two most mentioned monitoring tools are visits and mystery shopping.
- (256) Manufacturers also explain that the degree of customer services required from the retailers differs depending on a variety of factors. For example, they consider qualified customer advice to be more important for innovative, technically complex, high-value products than for simpler products. They also consider the provision of customer services, particularly at the pre-purchase stage to be important in terms of persuading customers that investing in a product will be worthwhile. Moreover, the provision of customer services at the retail level is considered the more relevant, the more premium, meaning prestigious, a brand is.

4.1.2.1 Types of customer services

- (257) As manufacturers explain, the type of customer service provided depends both on the nature and brand category of the product, but also on the sales channel.

¹⁵⁷ An important majority of manufacturers (74 %) indicated that this applies to most of their brands and products.

¹⁵⁸ 220 respondents consider value added customer services offered by retailers to be important for enhancing demand for most or some of their brands/ products.

¹⁵⁹ 59 % of the respondents who have indicated that customer services are important sell through selective distribution, while 50 % through exclusive distribution. 21 % have franchising agreements in place.

¹⁶⁰ Overall, 39 % (corresponding to 102 manufacturers) of the respondent 252 manufacturers do not monitor the services provided by retailers.

¹⁶¹ As outlined in paragraph (164)(166), 35 % of manufacturers indicate that they do not sell their products to pure online sellers.

- (258) When it comes to pre-sale services, independently of the product category and the sales channel, almost every respondent manufacturer underlines the key importance of providing expert advice to customers.
- (259) Manufacturers report that they require trained and knowledgeable personnel to explain the use/application and features in particular of technically complex products or provide dedicated personalised advice for more prestigious branded products. For technical products, it is also often required that the retailer invests in diagnostic and repair tools. Many respondents explain that they organise trainings for the retailer's personnel, where depending on the scheme, participation is either obligatory or financially incentivised.
- (260) Online, the advice and detailed product information is provided via product descriptions, product pictures (some of which high resolution and/or 360 degree) and videos presentations (either on their own website or on hosting sites), documents for downloading (such as user-guides technical specifications), product availability information, customer reviews and ratings, press reviews, blogs and newsletters, emails, chat services, and (multi-language) call-centres.
- (261) Manufacturers consider the adequate representation of the brands and products, both online and offline as key.
- (262) For offline sales, manufacturers' main requirements relate to shop design, decoration, specific installations, shop-in-shops, cleanness and attitude of the personnel. For instance, manufacturers explain that for premium cosmetics and clothing, it is crucial that customers can see, touch, feel, smell and experience the products in an environment that is in line with the brand image.
- (263) Manufacturers also explain that it is important that retailers which sell online, provide product presentation/demonstration through high quality images, videos and detailed explanations of the functioning and features of the product.
- (264) Some hybrid players explain that in their philosophy and business practice they do not see a major difference between offline and online pre-sale services. As one of them summarises: *"[...] we have specialized stores with knowledgeable staff, both offline and online. We spread information about our products both online (web shop, blog, social media, newsletter) and offline (in-store). Since we are a true omnichannel company the distinction between online and offline in our sales is not easy to make. We don't have a preference whether the customer informs itself online or offline or whether the customer buys online or offline. We feel that giving the customer both options without clearly steering them is the best way to get happy clients."*
- (265) Manufacturers consider after-sales services as particularly important for certain product categories, such as electronics and other long-life goods, both online and offline. Assembly, installation, data transfer from old devices, problem solving, products customer support by phone, service desks or service department for reclamations, recycling, warranty services and handling of customer queries, complaints and defects,

regular product and information updates, as well as spare part supplies are seen as important. Efficient handling of return of the purchased products; return/money-back guarantees and flexible return solutions are more important in case of online sales. Order tracking is another after-sales service specific to online sales.

4.1.2.2 *Financing of customer services*

- (266) The preliminary findings of the sector inquiry show that manufacturers compensate retailers for part of these customer services. Overall, 50 % of the respondent manufacturers¹⁶² declare to provide incentives to retailers to increase the provision or to improve the quality of customer services. About 24 % of the respondent manufacturers¹⁶³ declare to offer compensation to retailers for having an online shop or for services provided by the online shop and 10 % do so with respect to most of their retailers.
- (267) Offline service compensation patterns are similar to the online ones. 36 % of the respondent manufacturers¹⁶⁴ declare to offer offline service compensations and 10 % do so with respect to most of its retailers. 12 % of the retailers declare to obtain compensation for offline services and 11 % for online services at least from some manufacturers.
- (268) Based on the responses of retailers, incentives provided by manufacturers may take diverse forms that can range from material support (such as in-store materials, manuals, catalogues, marketing material, sample products); non-material support (in particular trainings) to financial support (for example rebates, bonuses or cost sharing schemes).
- (269) Manufacturers and retailers explain that manufacturers may provide financial support. Such support is either cost or performance-related and may take diverse forms and be linked to diverse conditions. Many manufacturers have marketing development funds to provide financial incentives for retailers to carry out promotion and advertisement activities. Manufacturers often set up a complex system of conditions which retailers must comply with to benefit from these funds.
- (270) Retailers also recurrently mention that manufacturers may provide incentives for promotion or marketing by either reducing the wholesale prices on certain products or providing direct payments that are often but not necessarily linked to turnover/sales volume. For instance, some manufacturers pay additionally for promotional banners on the website or for preferred product positioning whether on the retailer's website or in the brick and mortar shop. Some manufacturers grant a marketing cooperation budget for specific marketing campaigns. The budget is invoiced by the retailer at the end of the campaign.

¹⁶² 230 manufacturers have responded to the particular question.

¹⁶³ 252 manufacturers have responded to the particular question.

¹⁶⁴ 251 suppliers have responded to the particular question.

- (271) Some retailers also report that manufacturers finance advertisement campaigns/promotions by providing extra discounts for a limited quantity of products, in order to advertise them. They explain that they pass on the discount to the customers, in order to benefit from the extra attention and increased traffic that may lead to cross-selling of complementary products. Some explain that they benefit from indirect incentives to advertise more the products of a specific manufacturer in the form of back-end-rebate (a wholesale price reduction if they reach a set target). Many mention to have cost-sharing/cost-compensation/co-investment agreements.
- (272) In terms of non-financial support, retailers report that they benefit from trainings, technical assistance and advice, promotion events, workshops, point-of-sale marketing materials, in-store displays such as promotional stands, shop furniture; and sample products. Specific online marketing materials may include software, product care and installation descriptions, product photos and videos, and other commercial and brand contents.
- (273) Some manufacturers have a differentiated incentive scheme through the range of products that they make available to retailers. The higher the quality of the customer service offered by the retailer, the wider and more premium product range the retailer can have access to.
- (274) 43 % of the respondent manufacturers¹⁶⁵ expressly require retailers to invest in specific facilities or human resources related to selling their brands/products. Almost half of those manufacturers require such investments from most retailers, whereas the rest from only some retailers.
- (275) According to the respondent manufacturers, in many cases investment requirements are part of the criteria to be admitted to the selective distribution system. For others, they are included in distribution agreements as part of the obligations of the retailers. 79 % of manufacturers that require investment in specific facilities or human resources at the retail level have a selective distribution system in place, while 57 % have territorial exclusive distribution system.¹⁶⁶ Whether such investments can be characterised as relationship specific, giving rise to the so-called "hold-up problem" (see paragraph (34)) and, therefore, justifying certain vertical restraints to overcome possible underinvestment would normally require a case-by-case assessment.

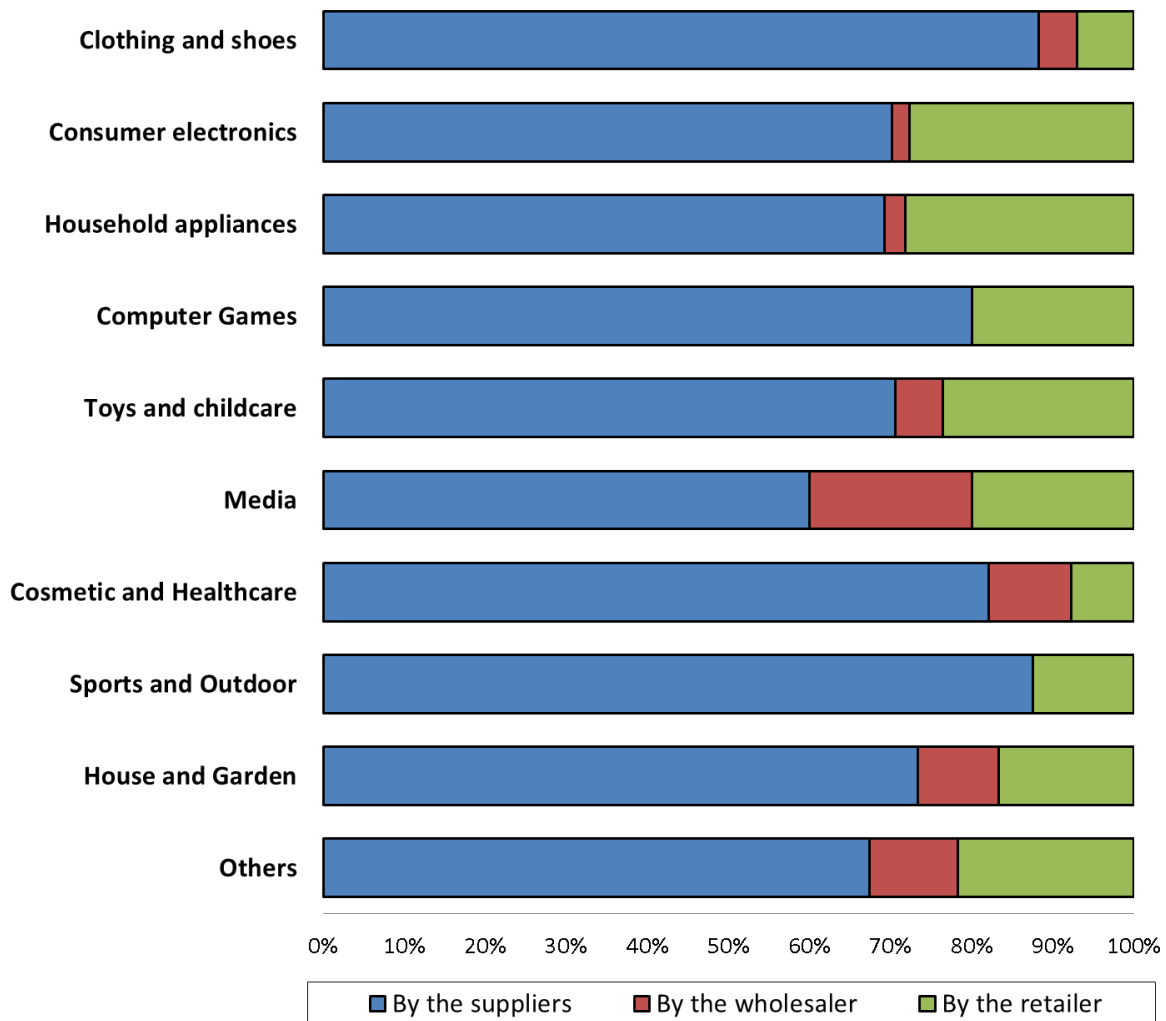
¹⁶⁵ Proportions are calculated on the basis of the 250 respondents to the question.

¹⁶⁶ Almost 90 % of the manufacturers who require investment in specific facilities or human resources at the retail level operate selective and/ or exclusive distribution system.

4.1.2.3 Promotion and advertising

- (276) To the extent that promotion and advertising at the retail level is important for attracting customers or conveying and maintaining a particular brand image, manufacturers may take measures to incentivise retailers to increase their promotion efforts, either through direct compensation or, indirectly, through making sure that retailers can appropriate the respective benefits.
- (277) As regards the level of the supply chain where most of the advertising and promotion takes place, no clear conclusion can be drawn from the responses of manufacturers and retailers. Manufacturers and retailers both believe that most of the advertising and promotion activity is typically undertaken at their respective level.
- (278) According to manufacturers, across all product categories, on average the manufacturers are mostly in charge of promotion and advertisement. With regard to specific product categories, relatively more manufacturers indicate that they are in charge of promotion and advertisement for clothing and shoes than for books, CD's and DVD's. In case of consumer electronics and household appliances almost one-third of the respondent manufacturers indicate that promotion and advertisement is mostly done by the retailers.

Figure B. 33: The proportion of manufacturers, wholesalers and retailers that typically carry out most of the advertisement and promotion per product category (based on the responses of manufacturers)¹⁶⁷



(279) The view of retailers differs from that of the manufacturers, as the great majority of them (on average roughly 80 %), independently of the product category, consider that most of the advertising and promotion is carried out by the retailers.

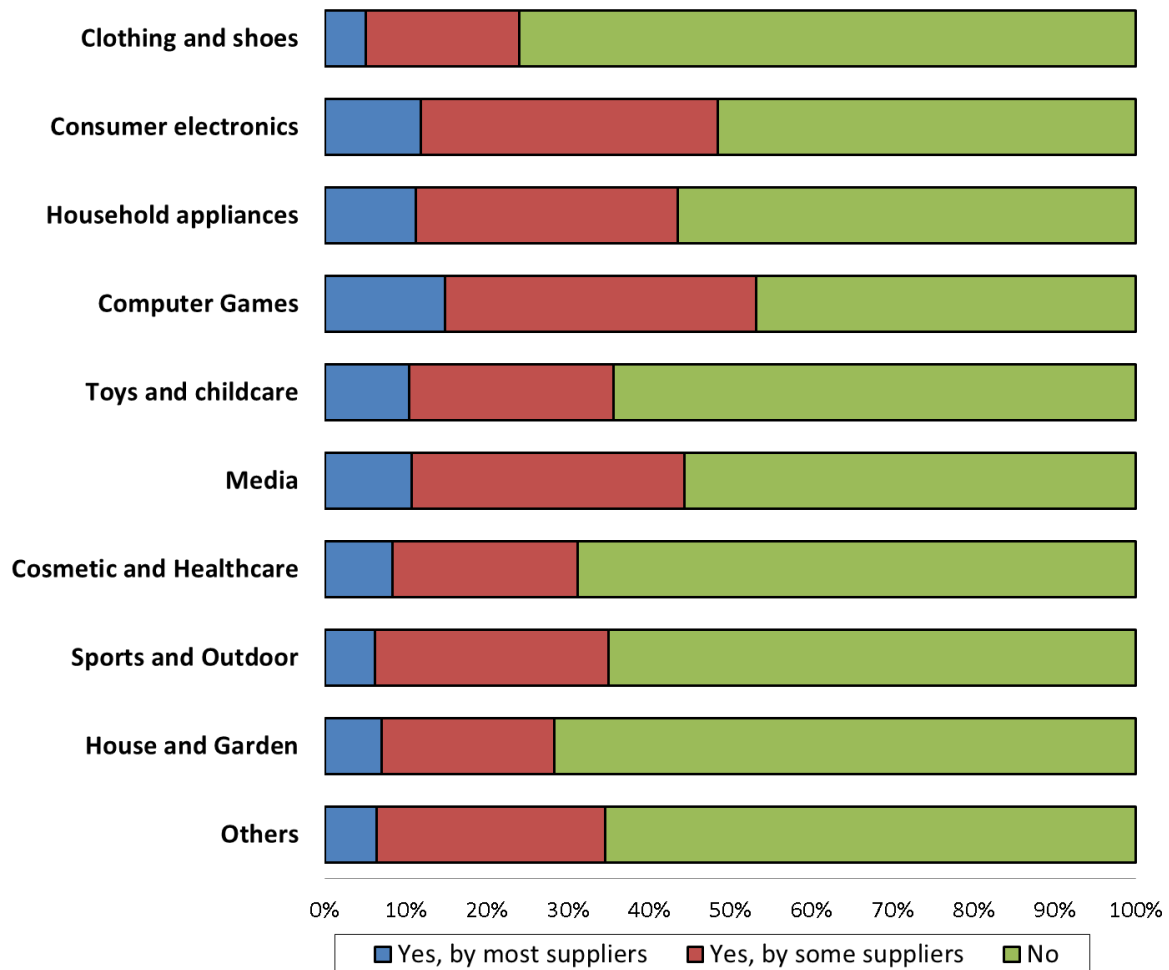
(280) These seemingly opposing views may be due to the different types of advertising and promotion that takes place at each level – manufacturers invest in promoting their brands, while retailers focus on the promotion of specific products. As one of the respondents summarises "[...] advertising in regard of demand creation is done by brand manufacturers alone (see for example generic TV product advertising) and the actual advertising for individual B2C products is done by the retailer".

(281) Retailers consider that in the majority of sectors manufacturers only provide incentives to advertise and promote to a limited extent. The responses of retailers indicate that

¹⁶⁷ The proportions are calculated on the basis of responses given per sector.

incentives are most important for computer games, as well as for consumer electronics and household appliances.¹⁶⁸

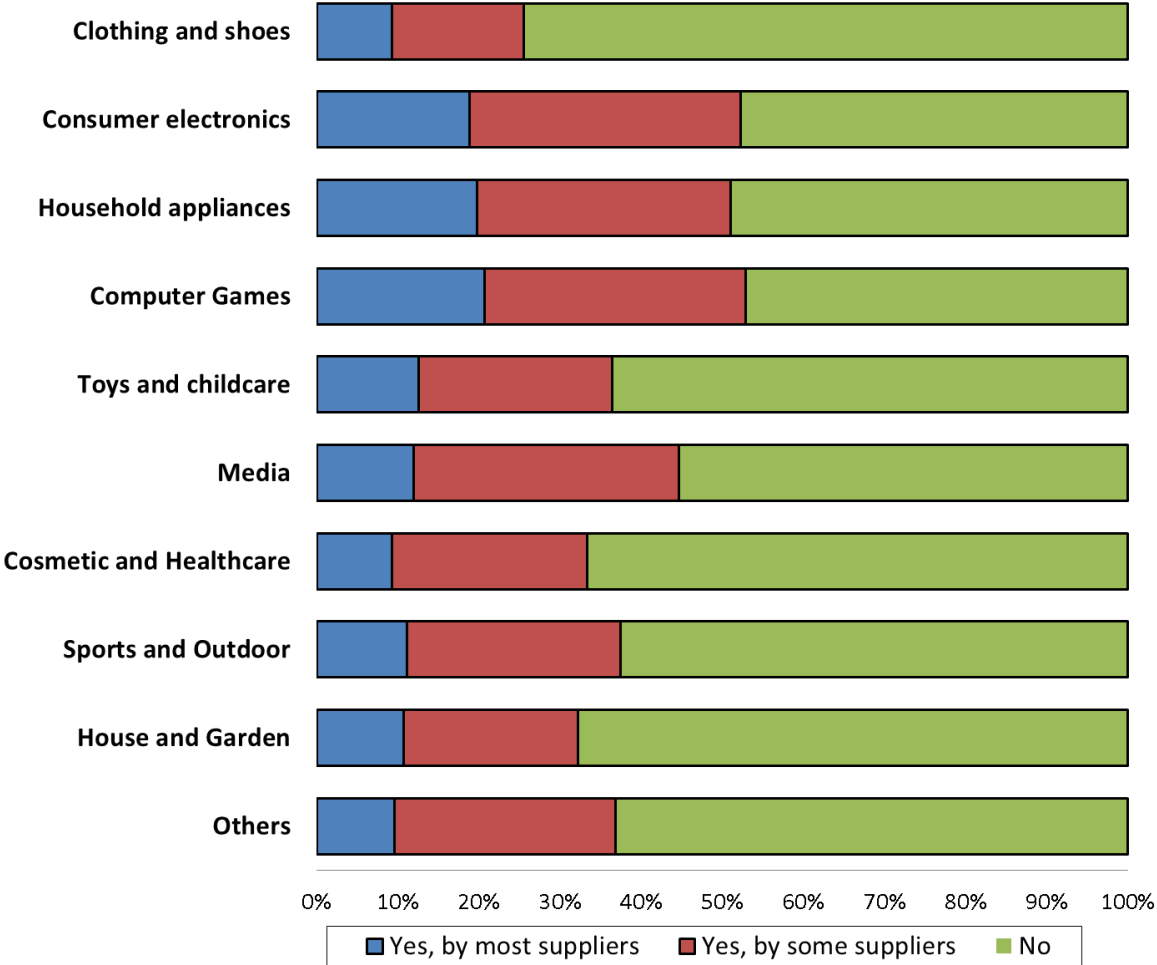
Figure B. 34: The proportion of retailers that report to be incentivised for advertisement and promotion online per product category (based on the response of retailers)¹⁶⁹



¹⁶⁸ Consumer electronics and household appliances are also the two product categories where, according to manufacturers, retailers are most involved in advertisement.

¹⁶⁹ The proportions are calculated on the basis of responses given per sector.

Figure B. 35: The proportion of retailers that are incentivised for advertisement and promotion offline per product category (based on the response of retailers)¹⁷⁰



(282) Somewhat more manufacturers state that they incentivise distributors for promoting and advertising offline (63 %)¹⁷¹ than online (51 %)¹⁷², whereas many indicate that they do not distinguish between the two channels (although among the listed compensations some are only meaningful for either offline or online sales). Many manufacturers explain that they set up complex multi-level marketing support and compensation schemes. The criteria to benefit from those schemes may advantage offline or online retailers. Few respondents explain that the Vertical Guidelines restrict their freedom to manage and compensate online and offline distribution channels independently.

4.1.3 Customers' purchasing behaviour and free-riding between the online and offline retail channel

(283) In view of the considerable efforts by both manufacturers and retailers in terms of offering customer services, promotion and advertising, the Commission assessed the

¹⁷⁰ The proportions are calculated on the basis of responses given per sector.

¹⁷¹ 252 manufacturers have responded to the respective question.

¹⁷² 253 manufacturers have responded to the respective question.

importance of free-riding between the offline and online retail channels¹⁷³, i.e. where customers benefit from services offered by one of the sales channels to make their choice, but then purchase the product via the other sales channel. Such customer behaviour and, hence, free-riding can be observed both ways.

- (284) Independently of the sales channel, customer services involve costs for the retailer that offers them. If following these customer services actual sales take place to a significant extent via other sales channels, it could reduce the incentives of retailers to invest in those services. As explained in section A.4., vertical restraints may be helpful in overcoming the free-riding problem.
- (285) While the Commission did not survey customers in the framework of the sector inquiry, it asked retailers and manufacturers to indicate, based on their business experience and knowledge, how prevalent "free-riding" between online and offline sales channels is, where customers benefit from services offered via one of the sales channels but carry out the actual purchase through the other channel. The Commission also asked respondents to describe the impact of free-riding on different aspects of their commercial decisions.
- (286) Overall, 45 % of respondent manufacturers indicate that free-riding, whereby customers benefit from services offered by brick and mortar shops to make their choice, but then purchase the product online is common (35 %) or very common (10 %). 27 % report that it is occasional and 2 % are of the view that it does not exist.¹⁷⁴
- (287) Quite similarly to the above figures, 42 % of the respondent manufacturers find that free-riding by offline retailers on services offered by online retailers (i.e. purchase in brick and mortar shops typically following online search) is common (32 %) or very common (10 %). 20 % of the manufacturers believe that the practice is occasional, while only 4 % indicates that it does not exist.¹⁷⁵
- (288) Free-riding by online retailers on services offered by brick and mortar shops is also acknowledged by the retailers: 7 % believe such behaviour is very common and 15 % that it is common. 21 % indicate that it is occasional, while 8 % are of the view that such behaviour does not exist.¹⁷⁶
- (289) The figures are fairly similar for free-riding by offline stores on services offered online: 8 % of the respondent retailers are of the view that such free-riding is very common and 14 % that it is common, 16 % believe that it is occasional, while 8 % are of the view that such behaviour does not exist.¹⁷⁷

¹⁷³ Free-riding concerns may also arise within the same sales channel. Such free-riding is however not the subject of this report.

¹⁷⁴ 26 % of the respondents do not know.

¹⁷⁵ 34 % of the respondents do not know.

¹⁷⁶ Half of the respondents say they do not know.

¹⁷⁷ More than half of the respondents say they don't know.

- (290) Although both manufacturers and retailers fully recognise the existence of free-riding in both directions, their comments show a greater sensitivity to the risks of free-riding by online retailers on the services offered by offline retailers.
- (291) The main reasons set out by both manufacturers and retailers are related to the costs of investment in brick and mortar shops which they claim are higher than the costs of investment in online sales. In particular, the premises (often required to be in city-centres or other higher priced areas, with specific requirements by the different manufacturers for the inside quality and arrangements of the shop), the specific facilities required by the manufacturers and human resources (in particular in qualified staff / training of staff) require substantial investments. Some manufacturers also emphasise the difference between free-riding by online retailers on offline services and free-riding by offline retailers on online services in terms of their impact on marginal cost. More specifically, the manufacturers claim that free-riding on services offered online would not increase the marginal cost of online players, while free-riding on the services offered by brick and mortar shops would increase the marginal costs of offline retailers.
- (292) A number of manufacturers as well as hybrid retailers point to a risk of seeing significant number of brick and mortar shops disappear, as a result of what they qualify as a general trend to use brick and mortar shops as "service providers", while making the actual purchases of goods via online sales channels, therefore directing to a large extent the money-flow to online retail.
- (293) The costs of online investments are also fully acknowledged by the respondents. The online retail investment costs that are most referred to are the costs of promoting the website, including search engine optimisation, platform commissions and online advertising, the costs (including human resources and software) of creating and maintaining the website, costs of maintaining a full online (interactive) catalogue on all websites, for all language versions, the costs of a call centre.
- (294) Manufacturers and retailers were asked about the way free-riding practices affected their business decisions. The trends described below represent the most typical ways to overcome free-riding between online and offline sales channels.
- (295) *Compensations*: as set out under paragraph (267), 36 % of manufacturers provide compensation to offline retailers for their offline shop and services, and the same proportion of manufacturers offers compensations to online retailers. Many manufacturers provide financial incentives and support to their retailers. Compensations for brick and mortar stores can typically depend on certain quality requirements, such as the offering of specific services or the presence of qualified staff. The financial incentives can take the form of bonuses, display discounts, exposure fees. The payment of a fixed fee to support offline sales efforts is one of the mentioned reactions to counter-balance the effects of free-riding. Compensations for online retailers are typically linked to the costs of online marketing / advertisement, to the marketing tools of the website, to the completeness of the information provided on the website, to the overall quality of the product display.

- (296) *Direct provision of material and training*: manufacturers and retailers equally report that manufacturers provide material to both offline and online retailers. To support offline retail, manufacturers provide "point of sale" material to brick and mortar shops, such as display furniture, marketing material, specific facilities or technology for shop design or for enabling optimised product presentation. To support online retail manufacturers provide digital tools such as digital catalogue, digital data for website content (photos, videos, all relevant data to optimise search), digital apps, marketing tools and material and buy keywords for search advertising. Many of the direct provisions of material form part of the obligations of manufacturers set out in the relevant distribution agreements.
- (297) *Recommended resale prices - online / offline price equivalence*: A harmonised online-offline resale price policy (whether by hybrid retailers or by manufacturers) is one of the most typical reactions to free-riding. Vertically integrated manufacturers state that they typically set equal prices online and offline, including equivalent discounts and promotional periods. Manufacturers also report about setting equivalent recommended resale prices to online and offline independent retailers as an attempt to limit free-riding. For the same purpose, several manufacturers explicitly state that they try to ensure harmonised retail prices across their online and offline distribution network.
- (298) Many retailers also report that they apply price equivalence across their online and offline shops to minimise free-riding concerns. The Commission asked hybrid retailers whether free-riding between sales channels affects their pricing decisions. More than 25 % of the respondent retailers report that free-riding by online retailers directly affects the prices they set in the different sales channels.¹⁷⁸ Similarly, 23 % of the respondent retailers report that free-riding by offline retailers affects the prices they set in the different sales channels.¹⁷⁹
- (299) *Ensuring overall equivalence online and offline*: beyond price equivalence, many manufacturers strive to maintain overall equivalence and consistency between online and offline to ensure a level playing field between those two channels. They state that they seek to maintain coherence of brand image on both sales channels, coherent design, equivalence of available product range, available product information, consistent product launch dates and marketing actions, and equivalent advertising messages. About a third of the respondent retailers indicate that free-riding across the two sales channels affects the range of brands and models they offer online and offline.¹⁸⁰
- (300) *Vertical integration / manufacturers entering into retail*: many manufacturers also report about increasing vertical integration as a reaction to free-riding concerns. With a view to keeping a better control over price and quality, some manufacturers decide to fully integrate distribution and manufacturing activities, and a significant number of manufacturers enter the retail level of distribution by opening their own retail websites

¹⁷⁸ Based on the responses of 163 retailers that answered the relevant question.

¹⁷⁹ Based on the responses of 162 retailers that answered the relevant question.

¹⁸⁰ 33 % out of the 163 respondents to the question regarding the impact of free-riding by online, and 31 % out of the 162 respondents to the question regarding the impact of free-riding by offline.

and/or brick and mortar stores. For more details on vertical integration, see section B.3.3 above.

- (301) *Changes in selective distribution / exclusion of pure online players*: to ensure a level-playing field between retailers, several manufacturers also state that they introduce the requirement in their selective distribution system for all retailers to run at least one brick and mortar shop. The exclusion of pure online players from the distribution network is one of the most commonly stated reactions to the concern of free-riding by online players. Also, many manufacturers explain that the amendments of their selective distribution criteria, namely the introduction of quality criteria for online sales and the focus on the equivalence of online and offline requirements also serve to ensure a homogenous brand image and a level-playing field between the two distribution channels.
- (302) *Requirement to sell a certain amount offline*: with a view to counterbalancing the impact of free-riding by online retailers and ensuring an efficient operation of the brick and mortar shops, some manufacturers request a certain absolute amount (whether in volume or in value) of sales via brick and mortar stores.
- (303) *Opening of showrooms*: to respond to the demand of both manufacturers and customers regarding the importance of offline shops, a number of initially pure online players report that they opened or intend to open showrooms or shops.

Summary

The preliminary results of the sector inquiry show that manufacturers attach high importance to product quality and brand image to attract customers and consider the price to be relatively less important. In turn retailers attach high importance to price as a parameter of competition. Building and maintaining brand image and quality reputation, according to manufacturers, is an important motivation for the implementation of different vertical restraints, such as marketplace restrictions, restrictions on the use of price comparison tools and recommended retail prices.

The majority of manufacturers consider that customer services at the retail level are important to enhance demand across product categories, independently of the sales channel (online or offline). Most of these manufacturers also sell via selective or exclusive distribution and/or provide recommended prices to retailers. Manufacturers employ complex schemes to provide financial and non-financial support to retailers in order to incentivise them to provide customer services.

Almost half of the respondent manufacturers expressly require retailers to invest in specific facilities and human resources related to selling their brands/products. Whether such investments can be characterised as client-specific, giving rise to the so-called "hold-up problem" and, therefore, justifying certain vertical restraints to overcome possible underinvestment, would require a case-by-case assessment.

Advertising and promotion activity takes place both at retail and manufacturing level. The preliminary findings show that retailers and manufacturers focus on different types of advertising. Manufacturers invest in promoting their brands, while retailers rather tend to promote specific products. About half of the manufacturers provide incentives to retailers to advertise and promote their products, with a higher proportion doing so vis-à-vis hybrid retailers.

Almost half of respondent manufacturers indicate that the practice, whereby customers benefit from services offered by brick and mortar shops in order to make their choice, but then purchase the product online (a situation, which gives rise to "free-riding"), was either common or very common. A slightly smaller proportion of respondent manufacturers find free-riding by offline retailers on services offered online (purchase offline following online search) also very common or common. The respondent retailers also confirm that free-riding takes place, although to a lesser extent. About a fifth of respondent retailers believe free-riding by online retailers on services offered offline is either very common or common and the same proportion of respondents indicate it is occasional. Figures are also largely similar for free-riding by offline retailers on services offered online.

Many respondents (both retailers and manufacturers) consider that the costs of investments in offline stores are higher than the costs of investments in websites. Compensation and direct provision of material to both sales channels, online/offline price-equivalence and overall coherence, vertical integration of manufacturers and changes to the selective distribution criteria, including the requirement of having at least one brick and mortar shop, are the most typical reactions to free-riding.

4.2 Overview of restrictions

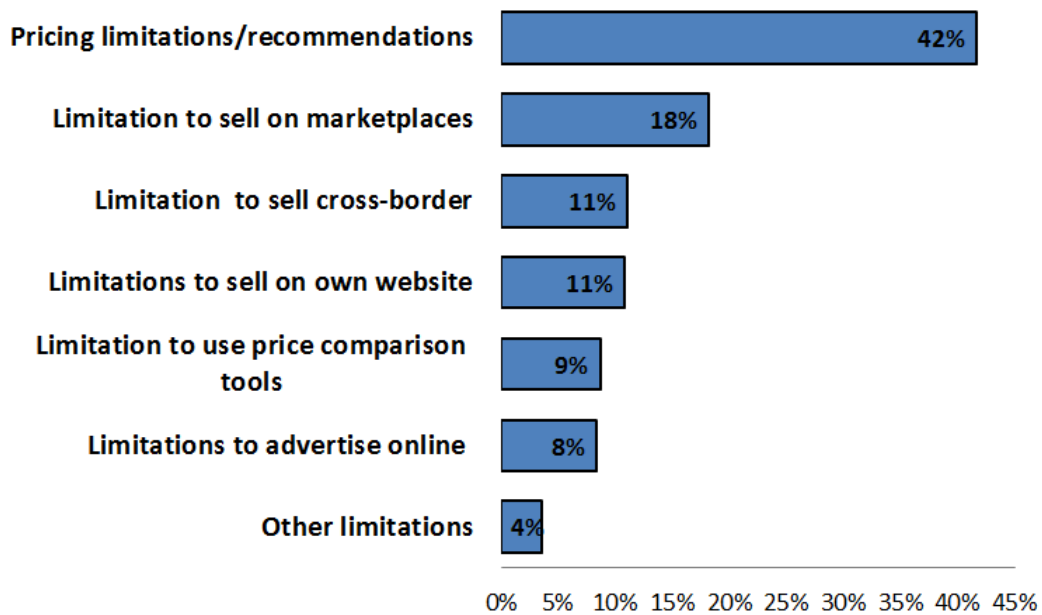
(304) This section of the Preliminary Report is dedicated to the analysis of restrictions of online sales of goods. It will in particular focus on a number of contractual¹⁸¹ restrictions which limit the retailers' ability to sell or advertise their products online.

(305) The restrictions analysed in this section should not be understood as an exhaustive list of restrictions. As new business models and market trends emerge other restrictions may be used by market players.

(306) Figure B. 36 below provides an overview of the prevalence of certain restrictions amongst retailers that participated in the sector inquiry and responded to the questionnaire.

¹⁸¹ For the purpose of this section "contractual" restrictions cover also restrictions by indirect means, i.e. situations in which a company is limited in its ability to sell or advertise online or set a certain price by means of warnings, threats, penalties, delay or suspension of deliveries or any other discouraging means, including financial incentives or disincentives, either in writing or orally, used to change the conduct of the company.

Figure B. 36: Proportion of retailers having contractual restrictions, per type of restriction¹⁸²



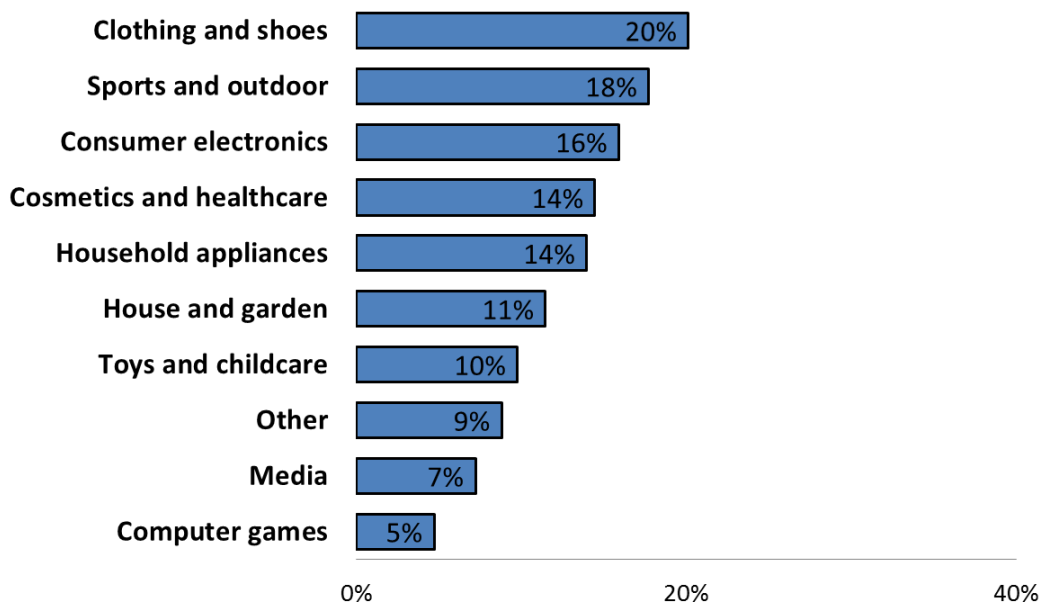
(307) Pricing restrictions/recommendations¹⁸³ are by far the most widespread restrictions reported by retailers. Restrictions on the use of marketplaces are the second most reported restrictions.

(308) All product categories are affected by restrictions although to a different extent. With the exception of media, computer games and software, at least 1 in 10 retailers active in each product category has experienced some form of restriction with respect to selling or advertising online. Clothing and shoes is the product category with the highest proportion of retailers having reported the presence of restrictions, followed by sports and outdoor equipment and consumer electronics.

¹⁸² Proportions are calculated out of all respondents (1051) to the retailers' questionnaire.

¹⁸³ Recommended retail prices are included in the list of pricing restrictions.

Figure B. 37: Proportion of retailers having at least one contractual restriction per product category¹⁸⁴



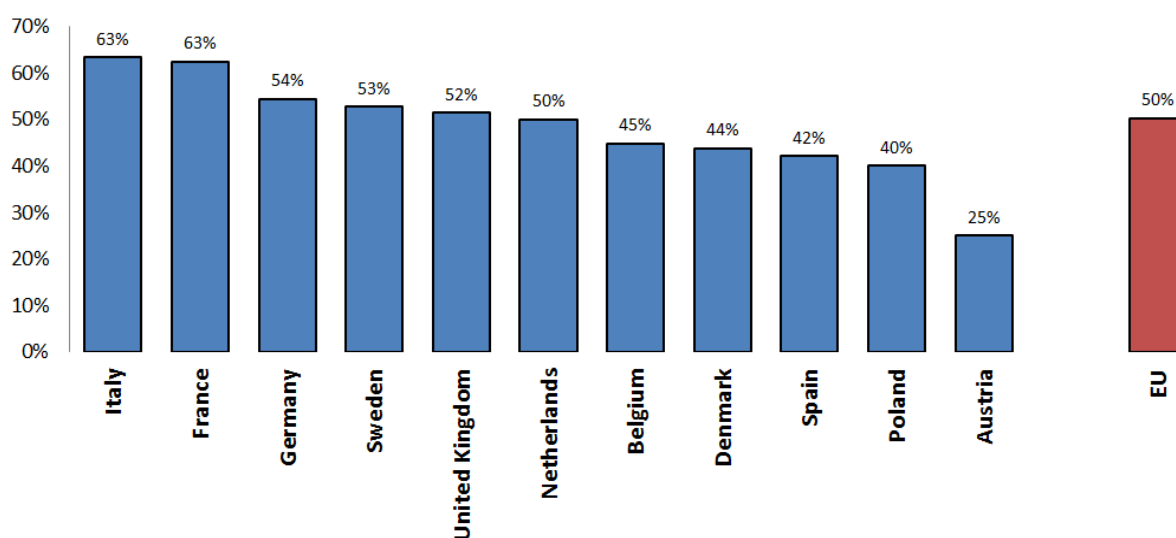
(309) Half of the respondent retailers report to be affected by at least one restriction to sell or advertise online.¹⁸⁵ In terms of geographic coverage, in all Member States retailers report to have at least one restriction to sell or advertise online. The figures below provide a snapshot of the contractual restrictions encountered by retailers in 11 selected Member States and across all product categories.¹⁸⁶

¹⁸⁴ Proportions are calculated on the basis of the number of respondents active in each product category.

¹⁸⁵ Many retailers are active in multiple product categories which is the reason why the product category specific proportions of retailers that have at least one restriction are not directly comparable to this overall proportion of retailers that have at least one restriction.

¹⁸⁶ Proportions are calculated on the basis of the number of respondents active in each Member State. Only Member States for which 20 or more retailers responded to the relevant question are presented in the figure.

Figure B. 38: Proportion of retailers having at least one contractual restriction per EU Member State



(310) In the following sections various restrictions will be discussed in more detail.

Summary

Pricing restrictions/recommendations are the most widespread contractual restrictions reported by retailers. Restrictions to use marketplaces are the second most reported restriction.

Half of the respondent retailers report to be affected by at least one contractual restriction to sell or advertise online.

All product categories are concerned by contractual restrictions although to a different extent: clothing and shoes is the product category with the highest proportion of retailers having reported the presence of contractual restrictions, followed by sports and outdoor equipment and consumer electronics.

4.3 Cross-border e-commerce and geographic restrictions to sell and advertise online

(311) Cross-border e-commerce has the potential of contributing to the integration of the EU's internal market as customers may find it easier to purchase products from another Member State online, rather than crossing the border and buying products in brick and mortar shops. Cross-border online purchases are however frequently not possible for customers, because retailers refuse to sell to customers abroad, for example by blocking access to websites, re-routing customers to websites targeting other Member States or by simply refusing to deliver cross-border or to accept cross-border payments.

(312) These measures are also known as "geo-blocking". Geo-blocking can be distinguished from "geo-filtering" measures, which refer to commercial practices whereby online retailers allow customers to access and purchase goods or services cross-border, but offer different terms and/or conditions depending on the location of the customer in a Member State different from that of the retailer.

(313) This section outlines first the geographic sales policies and activities of manufacturers and retailers. This is followed by a section where geo-blocking and geo-filtering practices by retailers are discussed as well as the potential commercial reasons for retailers not to sell cross-border. The last part of the section will present the preliminary findings on contractual cross-border sales restrictions.¹⁸⁷

4.3.1 Geographic sales strategies of manufacturers

(314) Manufacturers were asked to provide information about the way they set up their distribution networks in the EU.

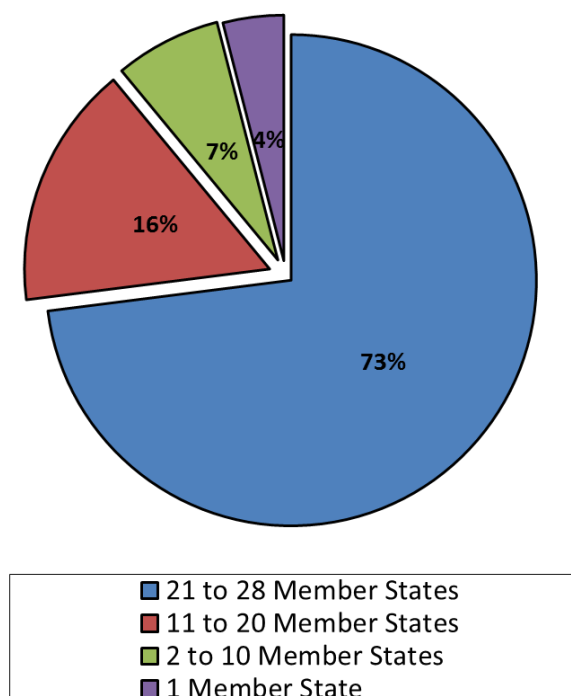
(315) Manufacturers reported a wide variety of distribution arrangements. Manufacturers can be grouped into two broad categories: the manufacturers that apply by and large the same distribution model across the EU and those that apply different distribution models depending on where their products are sold.

(316) Manufacturers that use different distribution models across the EU consider that certain markets/Member States have certain peculiarities in particular with regard to local customer tastes/preferences or habits or the market structure at the distribution level that require tailored approaches. For example, wholesalers may be an important intermediate level to ensure a broad geographic coverage in some Member States and be of lesser relevance in other Member States in which large retail chains provide for a good geographic coverage. A factor that manufacturers also take into account when deciding on the use of specific distribution models is the degree of development of e-commerce in a given Member State.

(317) Manufacturers were asked to indicate in how many EU Member States they sold their products in 2014 either directly or via independent wholesalers or retailers. As can be seen in Figure B. 39 the responses show that taking all product categories together the majority of manufacturers distributed their products in at least 21 Member States, while only a limited proportion (4 %) supplied them in only one Member State.

¹⁸⁷ In the framework of the sector inquiry, the Commission published in March 2016 its initial findings on geo-blocking in an Issues paper (See SWD(2016) 70 final). The initial findings of the Issues paper are confirmed by the Preliminary Report. However, as the Commission received some of the responses only after the data extraction date for the Issues paper, certain figures have been slightly modified.

Figure B. 39: Geographic scope of manufacturers' sales activity split by number of Member States (all product categories)¹⁸⁸



(318) The majority of manufacturers in each product category supplied their products in 21 to 28 EU Member States. The highest proportion of manufacturers selling in at least 21 Member States are those active in cosmetics and healthcare products followed by those that supply consumer electronics.¹⁸⁹

(319) Manufacturers explain that the strategy of selling directly to retailers without involving wholesalers is used in those Member States which manufacturers consider to be most important from a business perspective. Where in-depth knowledge of a given market in a Member State or territory is needed, manufacturers tend to sell via well-established wholesalers rather than directly to retailers.

(320) Manufacturers also use different types of distribution agreements to target specific Member States. Manufacturers may, for instance, use selective distribution agreements

¹⁸⁸ Proportions are calculated out of all 257 responses to the question. Respondents were asked to provide a separate response for each product category in which they are active. For manufacturers active in multiple product categories, the product category with sales into the highest number of Member States was considered as indicative of the presence of the manufacturer across the EU.

¹⁸⁹ 80 % of manufacturers of cosmetics and healthcare products reported selling their products in at least 21 Member States while the proportion of manufacturers of consumer electronics selling in the same number of Member States was 76 %. Proportions are calculated on the basis of the number of respondents active in each product category.

in some Member States in which their brand is well-established and use exclusive distribution agreements in Member State for products or brand(s) that are newly introduced and require specific sales efforts from distributors.¹⁹⁰

4.3.2 Geographic sales strategies of retailers and cross-border e-commerce

(321) Geographic sales strategies of retailers vary significantly amongst the respondents to the retailers' questionnaire.

(322) Many retailers focus their sales activity on a single Member State and their respective website is targeting customers in this Member State only. Others try to expand their activity into other Member States (for example by selling cross-border via an existing website or a marketplace or by launching a new website targeting specifically customers in another Member State).

4.3.2.1 Retailers not selling cross-border

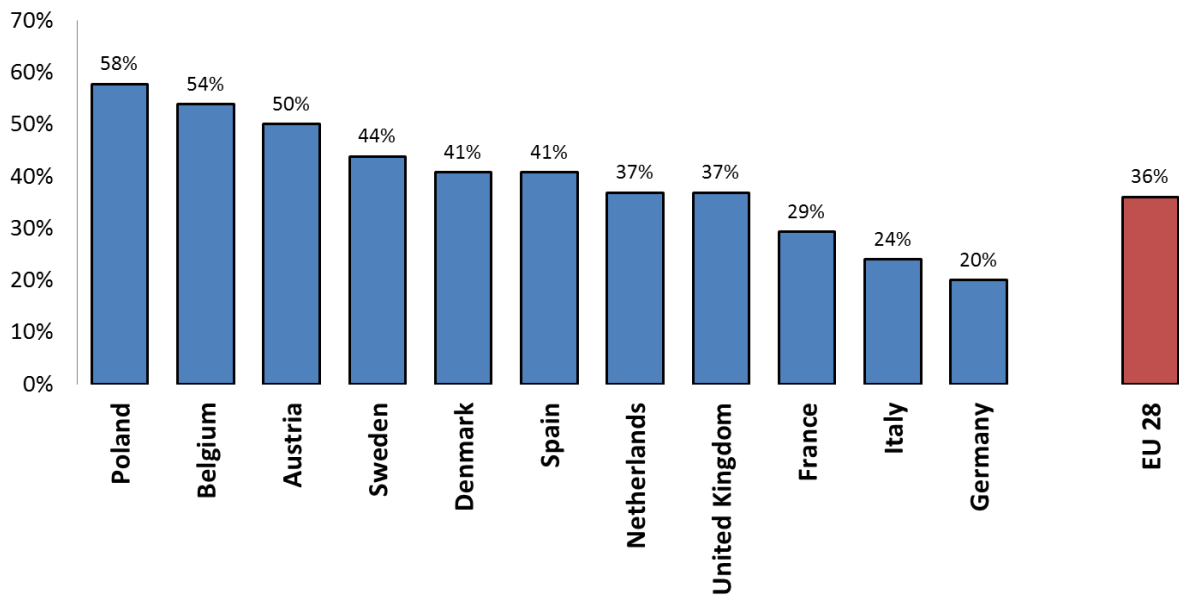
(323) 36 % of retailers that responded to the relevant question report they do not sell cross-border for at least one of the relevant product categories.¹⁹¹ Across the 28 EU Member States the median proportion of the retailers that report that they do not sell cross-border for at least one of the relevant product categories is 47 %. This means that for half of the Member States this proportion is below 47 % and that for the other half it is above 47 %.

(324) At Member State level, the proportion of respondents that do not sell cross-border is typically lower for larger online markets, such as France and Germany, compared to smaller markets, such as Belgium, where retailers reported to focus more on national sales. Figure B. 40 below provides an overview of the proportion of respondents that report that they do not sell cross-border in at least one product category in each Member State.

¹⁹⁰ See also section B.3.4.2 *Territorial exclusive distribution agreements* where territorial exclusivity is discussed and section B.3.4.3 *Selective distribution* where selective distribution is analysed.

¹⁹¹ Proportions are calculated out of all 918 respondents to the relevant question.

Figure B. 40: Retailers that do not sell cross-border in at least one product category for selected Member States¹⁹²

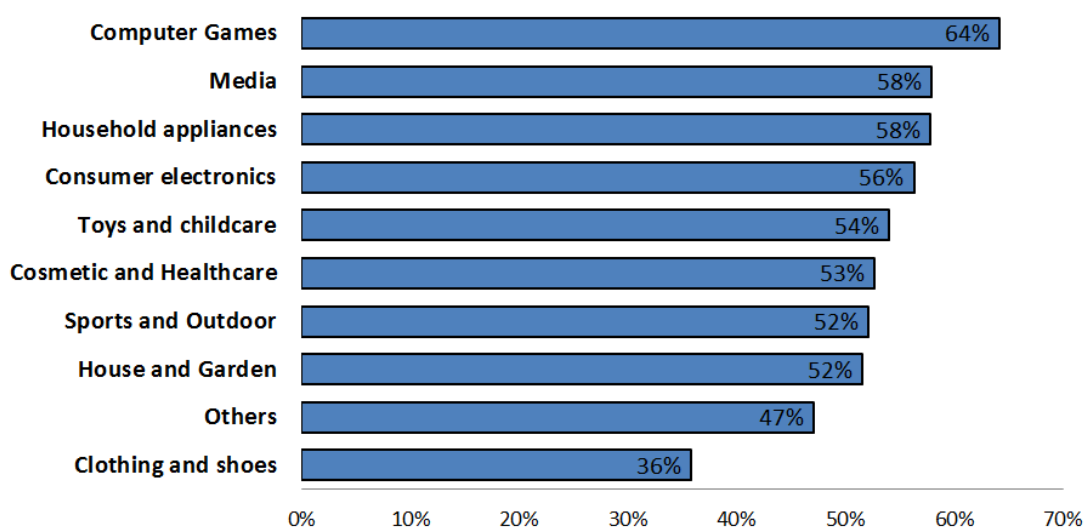


(325) The decision of a retailer not to sell cross-border does not appear to be related to the product category sold. As can be seen from Figure B. 41 below, in all product categories apart from clothing and shoes, more than half of the respondents that replied to the relevant question in relation to the respective product category reported that they do not sell cross-border.¹⁹³

¹⁹² Proportions are calculated out of all respondents that replied to the relevant question and are active in a given Member State. Only Member States for which 20 or more retailers responded to the relevant question are presented in the figure.

¹⁹³ The proportions for each product category are calculated out of all respondents that replied to the relevant question for a given product category. A single respondent can be active in several product categories and was therefore able to provide a separate reply for each of the product categories in which it is active. It follows that, as the basis for the calculation is different, these proportions are not directly comparable to the proportion of respondents (i.e. 36 %) that reported not selling cross-border in at least one product category. The number of respondents to the relevant question ranges from 488 in clothing and shoes to 221 in the category "others".

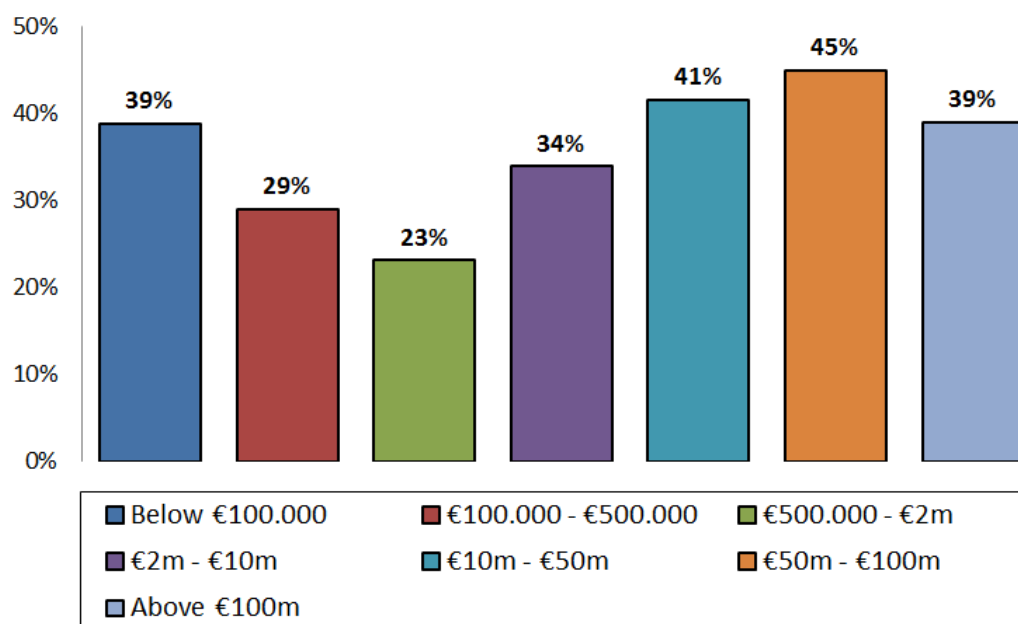
Figure B. 41: Retailers that do not sell cross-border for each product category



(326) The proportion of retailers not selling cross-border in at least one product category is slightly higher in the higher turnover categories. More than a third of respondents in the turnover categories above EUR 2 million indicated that they do not sell cross-border in at least one product category. Larger retailers active in several Member States often decide not to sell cross-border from a given website, but rather to establish/buy a new country-specific website in order to target customers in another Member State.¹⁹⁴

¹⁹⁴ As explained in paragraph (48), retailers were asked to provide separate responses for each of their websites. If a retailer has indicated that it does not sell cross-border from a particular website, it does not mean that the retailer is not present and selling its products abroad via a different website.

Figure B. 42: Retailers that do not sell cross-border in at least one product category for each 2014 turnover category¹⁹⁵



4.3.2.2 Cross-border visits and transactions on retailers' own websites

(327) In order to assess the extent of cross-border business activity amongst retailers, in terms of both cross-border visits and transactions, retailers were asked to provide information about the number of visits to their websites and the number of purchases that were made in 2014 from customers located in each Member State.

(328) Altogether the average proportion of visits coming from other Member States (as opposed to domestic visits¹⁹⁶ is approximately 20 % of all visits in the EU, across all respondents that provided the relevant information.¹⁹⁷

(329) At Member State level, the proportion of visits from abroad varies greatly, as can be seen from the figure below. This is also due to the fact that the number of visits is to a certain extent influenced by the size of the population. Therefore, even in traditionally larger e-commerce markets such as Germany and the UK, the proportion of visits from abroad is relatively modest compared to the proportion of domestic visits. A high proportion of cross-border visits was reported for some of the Nordic Member States.¹⁹⁸

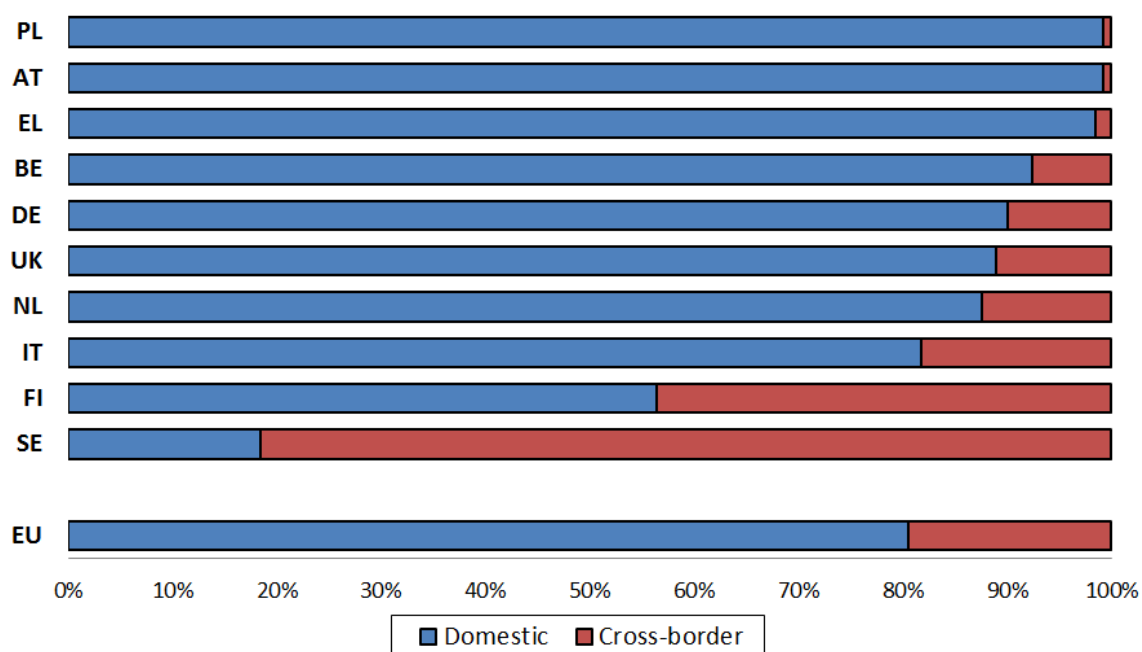
¹⁹⁵ Proportions are calculated out of all respondents in a given turnover category that replied to the relevant question. The number of retailers per turnover category that responded to the question range from 69 in the turnover category EUR 50 million to EUR 100 million to 267 for the turnover category above EUR 100 million.

¹⁹⁶ Domestic visits are visits from the Member State that the website targets.

¹⁹⁷ 750 respondents provided data on the number of visits that occurred in 2014.

¹⁹⁸ The percentages in individual Member States may be influenced by the existence of large retailers (some of which operate a single website to serve customers in multiple Member States) driving the Member State average.

Figure B. 43: Proportions of domestic and EU cross-border visits on retailers' own website in 2014 per Member State¹⁹⁹



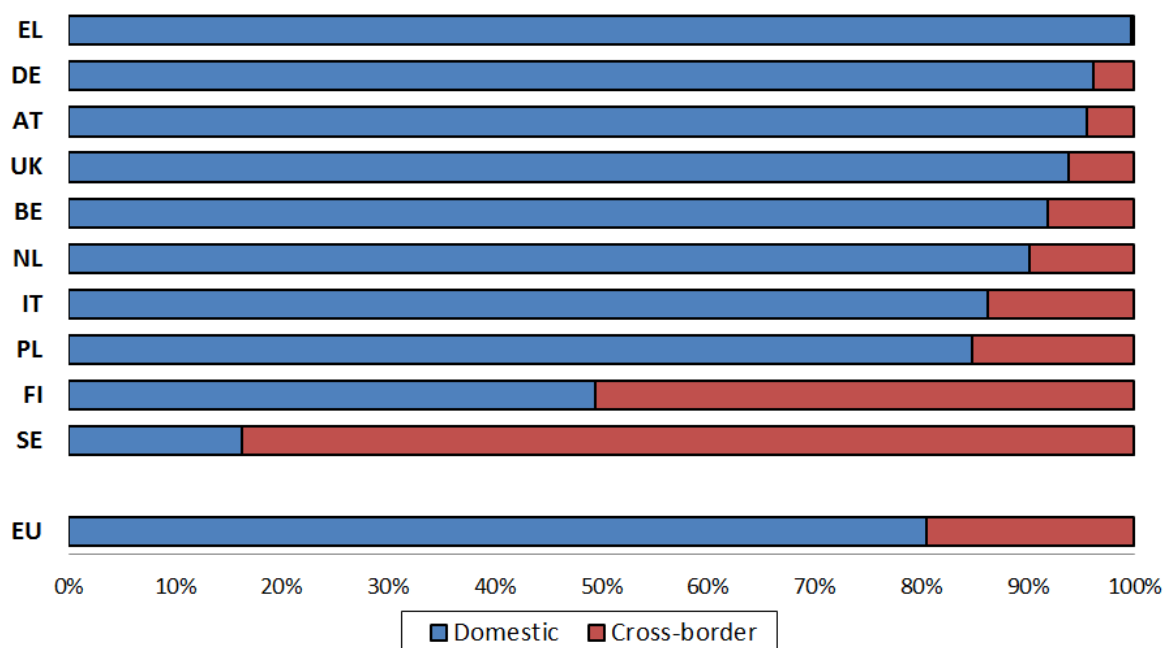
(330) Looking at actual purchases, 55 % of respondents²⁰⁰ report that all their customers were located in one Member State, while 12 % sold to customers located in 26 or more Member States. On average, the proportion of EU cross-border purchases reported by respondents is the same as the proportion of EU cross-border visits, namely approximately 20 %. Also in the case of purchases, the size of the population of a Member State is one of the elements that may influence the relationship between domestic and cross-border purchases.²⁰¹

¹⁹⁹ Only Member States for which 20 or more retailers responded to the relevant question are presented in the figure.

²⁰⁰ Proportions are calculated out of all respondents (744) that provided data on the number of purchases that occurred in 2014.

²⁰¹ The percentages in individual Member States may be influenced by the existence of large retailers (some of which operate a single website to serve customers in multiple Member States) driving the Member State average.

Figure B. 44: Proportions of domestic and EU cross-border purchases on retailers' own website out of all purchases in 2014 per Member State²⁰²



4.3.2.3 The role of online marketplaces for cross-border sales

(331) Marketplaces typically allow retailers to choose whether they want to deliver abroad.²⁰³ Marketplaces may make it easier for companies to sell cross-border for a number of reasons. Sellers that want to increase sales into another Member State may be able to do so without incurring the cost of launching a new dedicated website for this Member State. Moreover, some marketplaces facilitate cross-border delivery or provide advice on the applicable rules when selling cross-border.

(332) Information received from retailers in the context of the sector inquiry suggests that marketplaces indeed facilitate cross-border sales and that retailers that sell (also) via marketplaces are more likely to sell cross-border compared to those which only sell via their own website. Approximately 44 % of retailers that sold only via their own website reported not to sell cross-border (in any product category), whereas approximately only 20 % of retailers that sold only or also on marketplaces reported not to sell cross-border.²⁰⁴ Moreover, approximately two thirds of the marketplaces report to be open to professional sellers from all 28 Member States.

²⁰² Only Member States for which 20 or more retailers responded to the relevant question are presented in the figure.

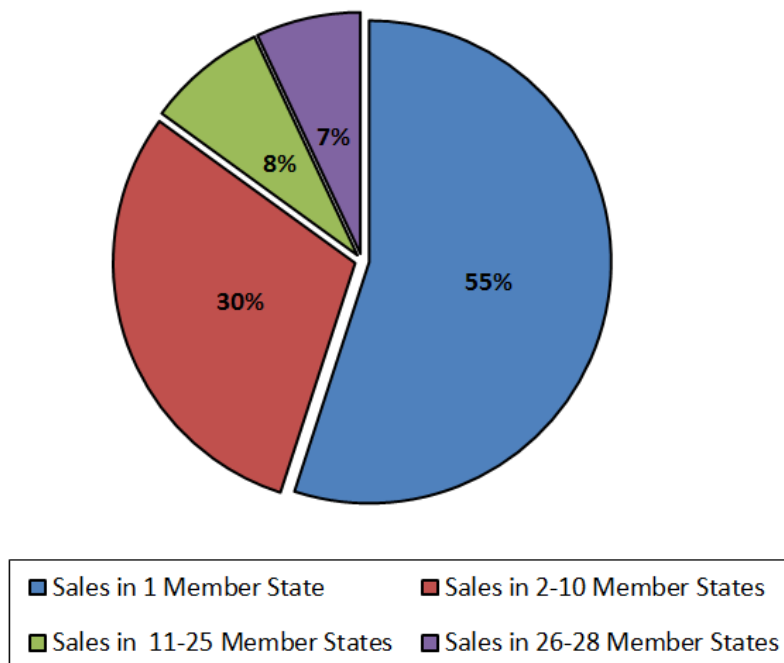
²⁰³ 84 % of the 32 marketplaces that responded to the relevant question report that sellers may choose the list of Member States they would like to deliver to. This choice was available either in general, that is for all products offered by a seller, or on a product-by-product basis.

²⁰⁴ The proportions are calculated on the basis the respondents that replied to all relevant questions and sell via own websites (namely 554 respondents) or marketplaces (312 respondents).

(333) On the other hand, information received from retailers in relation to actual purchases on marketplaces as well as information received from marketplaces indicates that approximately half of the sellers on marketplaces choose to sell into one Member State only and not sell cross-border.

(334) The Commission asked retailers to provide information on the number of purchases completed via marketplaces by buyers located in each Member State. 55 % of retailers that provided this information indicate sales to buyers in one Member State only.²⁰⁵ 45 % of retailers report that they sold products to buyers in two or more Member States out of which 7 % report to sell their products via marketplaces to 26 or more Member States.

Figure B. 45: Retailers indicating purchases that occurred via marketplaces in 2014 split by geographic coverage



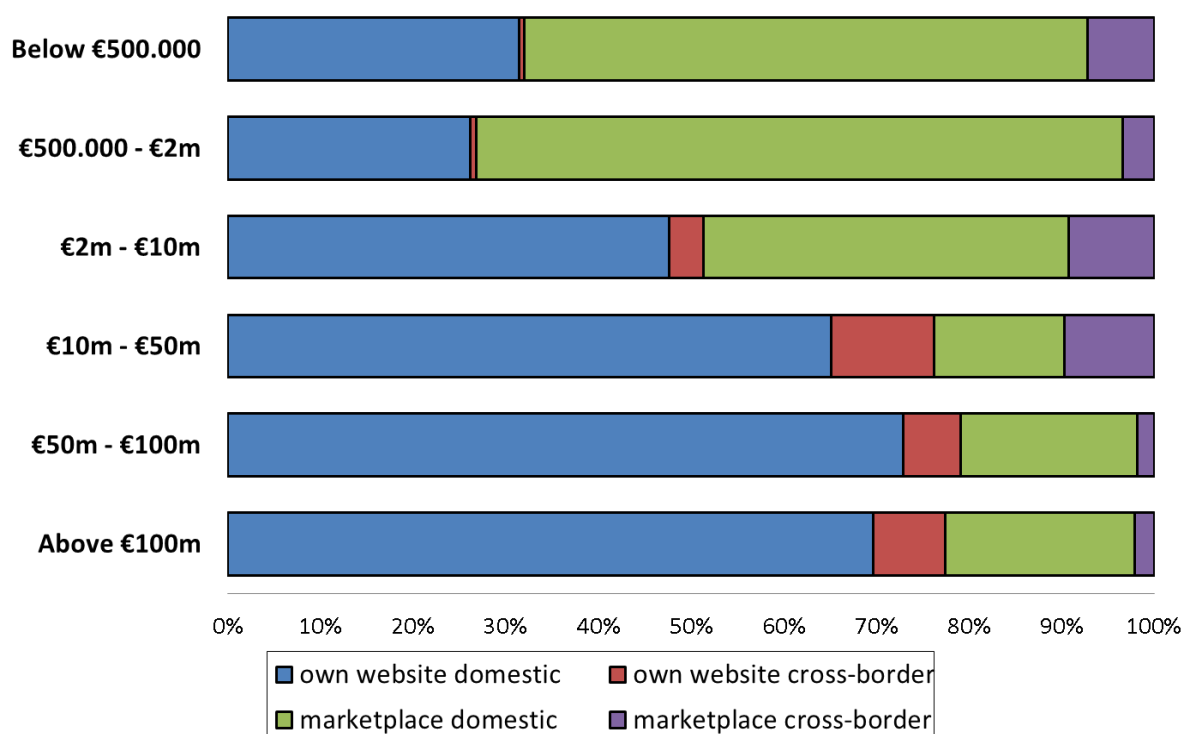
(335) Marketplaces report that on average in 2014 approximately 28 % of sellers chose to make their goods available for delivery to at least 21 Member States while 51 % chose to have their goods delivered to one Member State only.²⁰⁶

(336) The figure below provides an overview of the average proportion of domestic and cross-border transactions completed in 2014 by retailers on their own website as well as on marketplaces. It shows that websites of large retailers achieve a higher proportion of cross-border transactions with customers located in other Member States compared to the websites of smaller and medium-sized retailers.

²⁰⁵ 213 respondents provided information on purchases that occurred via marketplaces.

²⁰⁶ The proportions are calculated on the basis of 25 respondents that replied to the relevant question.

Figure B. 46: Average proportion of retailers' sales on own website and on marketplaces, domestic and cross-border²⁰⁷



(337) The average proportion of cross-border sales via marketplaces is significantly higher than the proportion of cross-border sales via the own website for retailers which achieved a total turnover of less than EUR 10 million, whereas it is lower for all turnover categories above this threshold. This suggests that marketplaces represent an important gateway for smaller and medium-sized retailers to sell cross-border whereas they are less relevant for cross-border sales of large retailers with a turnover above EUR 50 million.

4.3.2.4 The role of price comparison tools for cross-border sales

(338) Another way for retailers to make customers aware of their online offering both domestically and abroad is using price comparison tools. Price comparison tools have adopted a business model that supports retailers' visibility also outside the Member State where the price comparison tool is established.

(339) The majority of price comparison tools allow customers to compare offerings across retailers active in different Member States. 60 % of the 83 price comparison tools that responded to the relevant question stated that they provide information about product listings from retailers that are active in Member States other than the Member State the price comparison tool is targeting. Almost two thirds of those price comparison tools

²⁰⁷ 168 respondents provided sales information on purchases that occurred both via their own web shop and marketplaces. The number of respondents in the turnover categories ranges from 21 in the turnover category EUR 50 million to EUR 100 million to 40 in the turnover category above EUR 100 million.

that list products from retailers based in other Member States also inform their potential customers upfront of the location of the seller.

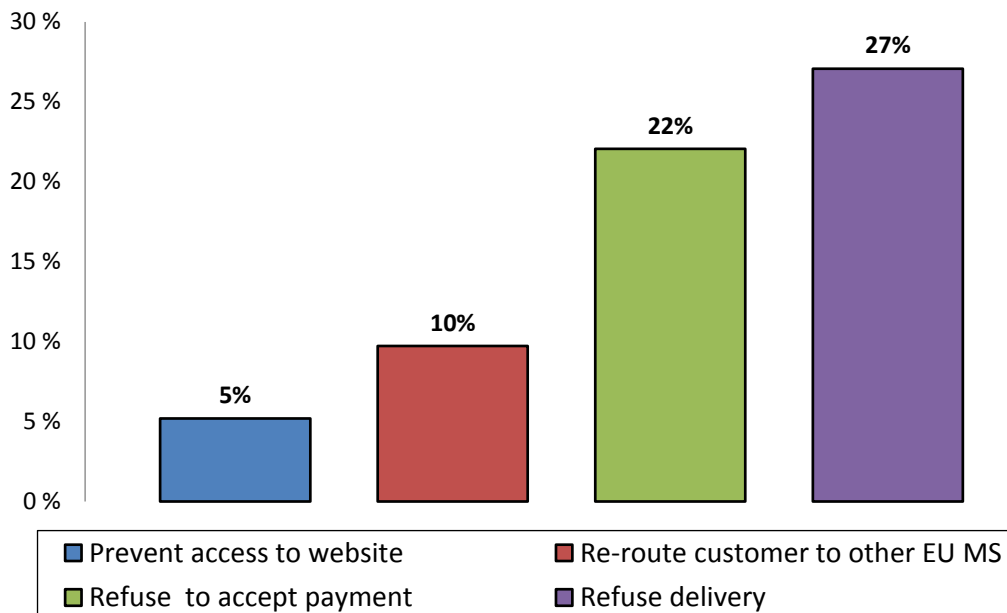
4.3.2.5 Geo-blocking measures

(340) In case retailers do not sell cross-border or do not sell cross-border into particular Member States they may implement the following geo-blocking measures in order to reject cross-border purchase requests: (i) prevent the customer from accessing the website, (ii) automatically re-route the customer to a website targeted at another Member State, (iii) refuse payment or (iv) refuse delivery. Each of these measures may be implemented by a retailer either unilaterally or as a consequence of an agreement with its supplier(s).

(341) Retailers usually collect some type of information about the location of customers. They do so for a variety of reasons, including, delivering goods or verifying that orders are legitimate. Retailers were asked whether they gather any location related information from (potential) customers (e.g. IP address, credit/debit card details) for geo-blocking purposes.

(342) The percentage of respondents at EU level that collects such data for geo-blocking purposes is 38 %.²⁰⁸ The figure below provides an overview of the proportion of respondents that use information about (potential) customers' geographic location for each of the geo-blocking purposes.

Figure B. 47: Retailers that gather location information for each geo-blocking purpose – EU 28²⁰⁹



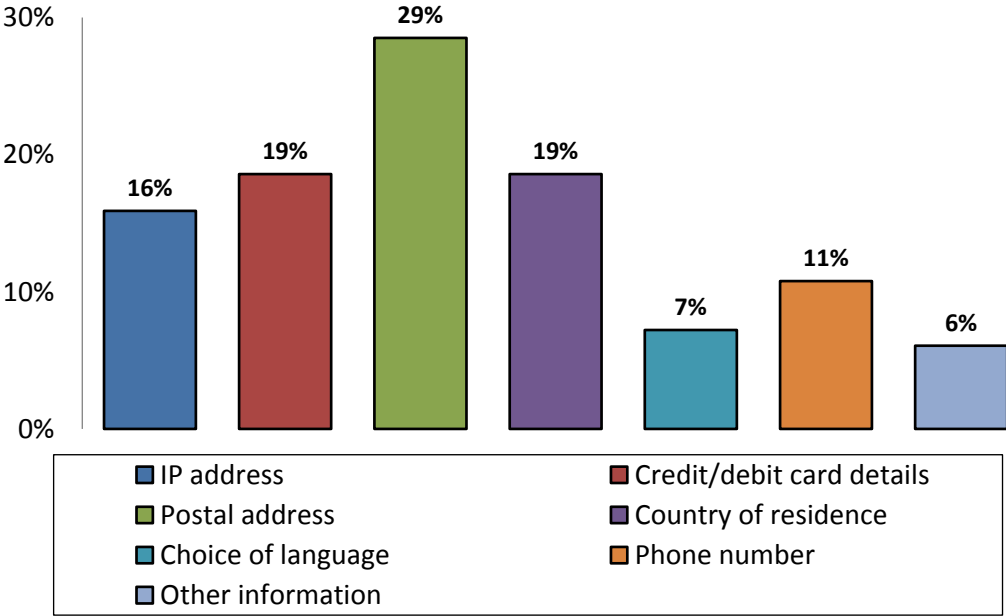
²⁰⁸ The proportions are calculated out of all 1051 respondents that replied to the retailers' questionnaire.

²⁰⁹ A single respondent was able to select multiple types of purposes for which it gathers location information.

(343) To implement geo-blocking, retailers collect various types of information on the location of the customer. The type of information that respondents most commonly collect for geo-blocking purposes is the postal address of the customer, followed by the customer's credit/debit card details or country of residence.

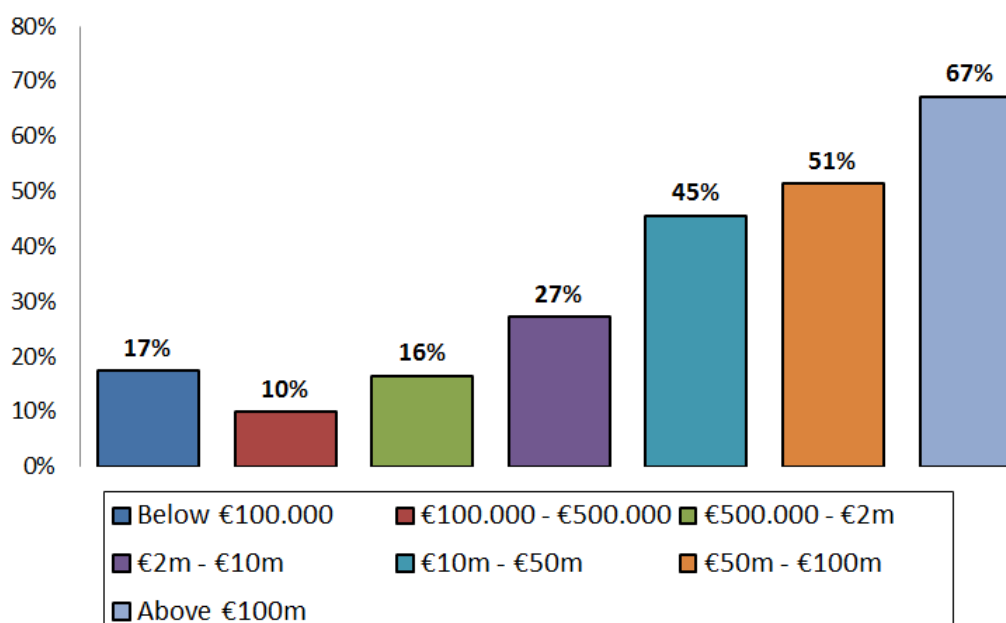
(344) The figures below show the proportion of respondents that gather location information for geo-blocking purposes per type of information and per 2014 turnover category of the respondents, respectively.²¹⁰

Figure B. 48: Retailers that gather location information for geo-blocking purposes, per type of information – EU 28



²¹⁰ Note that a single respondent was able to select multiple types of location information which it gathers.

Figure B. 49: Retailers that gather location information for geo-blocking purposes for each 2014 turnover category²¹¹



(345) There is a positive correlation between the total turnover and the proportion of respondents that gather location information for geo-blocking purposes. With the exception of the lowest turnover bracket, the higher the turnover, the higher the proportion of retailers that gather information for geo-blocking purposes. The reason for this may partly be that respondents in the higher turnover categories are more likely to have visits by (potential) customers located in another Member State.

4.3.2.6 Geo-filtering and cross-border price and offer differences

(346) The Commission also analysed the extent to which geo-filtering practices are applied by retailers. Retailers were therefore asked whether they charge different prices when they sell the same product cross-border to any Member State other than the one in which their website is established.

(347) Approximately, three quarters of respondents that sell cross-border indicated that they do not charge different prices for such sales, whereas one quarter of respondents indicated that they charge different prices at least for some products.²¹² The majority (79 %) of retailers that provided information about margins that they obtained from

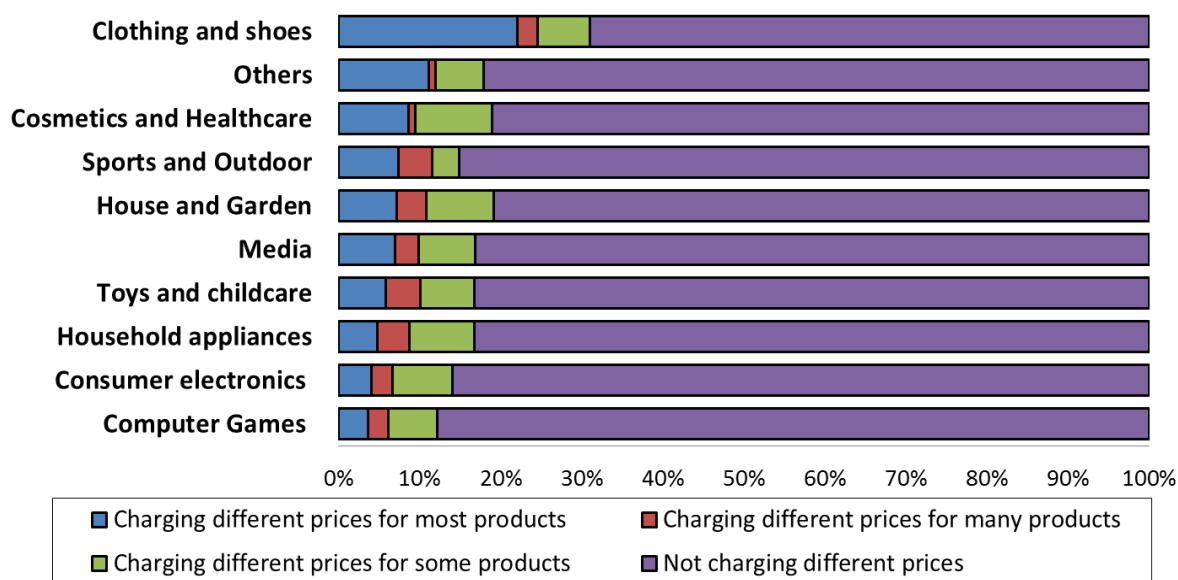
²¹¹ Proportions are calculated out of all respondents that replied to the retailers' questionnaire in a given turnover category.

²¹² The proportion of respondents is calculated out of all respondents that sold cross-border and that replied to the respective question (603 retailers). As retailers were asked to provide separate responses per operated website, the responses received do not provide information on price differences applied by retailers when selling products at different prices on different websites.

cross-border sales reported they did not achieve different profit margins for the same product depending on whether it is sold cross-border to another EU Member State.²¹³

(348) Figure B. 50 below shows the proportion of respondents that reported that they charge a different price for the same model of a product brand when selling cross-border to any EU Member State other than the one in which their website is established.²¹⁴

Figure B. 50: Respondents that charge different prices (excluding delivery costs) when selling cross-border, in each product category at EU level



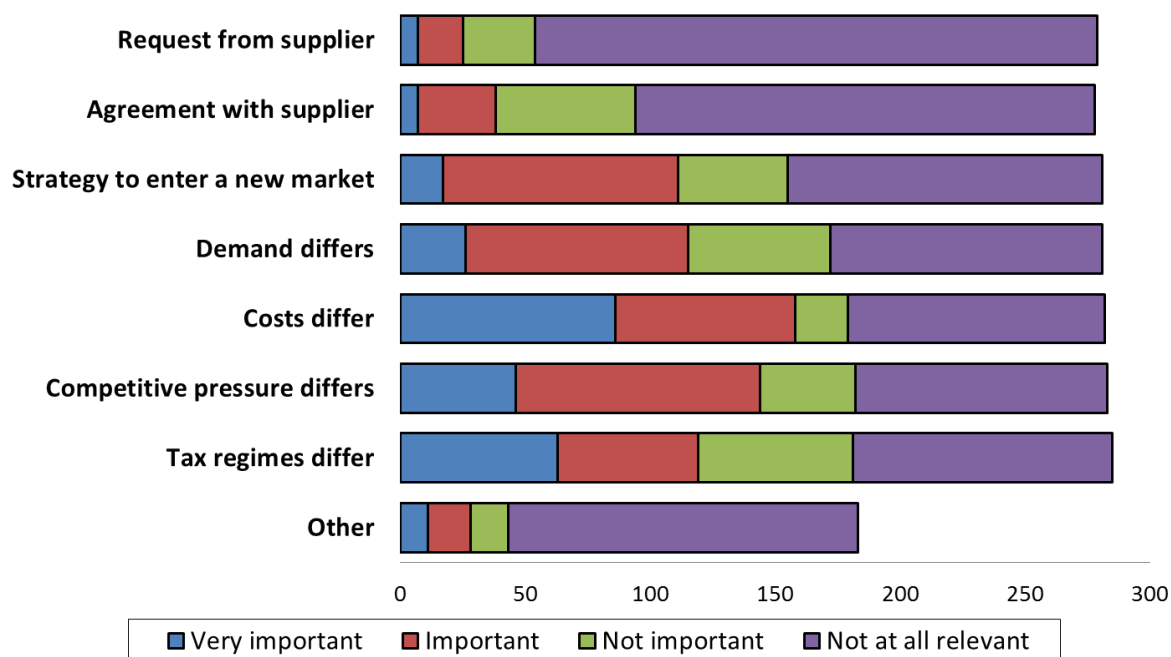
(349) The product category in which the highest proportion of retailers charges different prices is clothing and shoes, where 31 % of retailers reported that they charge different prices out of which 22 % charge different prices for the large majority of products offered.

(350) Retailers that charge different prices when selling cross-border were questioned about the main reasons for doing so. They were requested to indicate the level of importance of a number of predefined reasons. The reasons that were considered most important were different tax regimes, costs and product demand as well as differing competitive pressure in other markets. Requests by manufacturers were considered less relevant.

²¹³ Proportions are calculated of the 723 respondents that answered the relevant question.

²¹⁴ Each respondent can be active in several product categories and was therefore able to provide a reply for each product category in which it is active. The proportions below are calculated on the basis of all of the respondents that sell cross-border and that replied to this question for the given product category. The number of respondents in the product categories range from 313 in the product category clothing and shoes to 82 in the product category computer games and software.

Figure B. 51: Number of retailers indicating the level of importance of pre-defined options for charging different prices when selling cross-border²¹⁵



(351) It emerges from the responses to the marketplaces' questionnaire that charging different prices for cross-border sales is not common when retailers sell their products via marketplaces. Only one out of 33 marketplaces that responded to the relevant question reported observing price differences in some product categories for the same product model sold by sellers on their platform cross-border to any Member State other than the one in which the professional seller is established.

(352) Manufacturers were also asked whether the products they supply differ in terms of characteristics depending on the intended Member State of sale. The majority of manufacturers report that their products would not differ while slightly less than a quarter of the respondents reported that there were differences but only in relation to some of the products.

(353) That said there are appreciable differences reported between product categories. In the product categories clothing and shoes as well as sports and outdoor equipment over 85 % of the manufacturers report that there are no differences between the products they supply depending on where the product is sold. In other categories, such as consumer electronics and household appliances, over 45 % of manufacturers report that their products differ depending on where they are meant to be sold²¹⁶. The main reasons

²¹⁵ Based on responses of overall 291 retailers.

²¹⁶ All proportions are calculated out of all respondents active in the product categories and that replied to the relevant question. In total, 251 suppliers provide information on whether their product characteristics would differ depending on where the product would be sold. Respondents could provide separate responses for each product category they are active in.

reported to explain those differences are technical requirements, such as different plugs for products sold in certain Member States or local customer preferences.

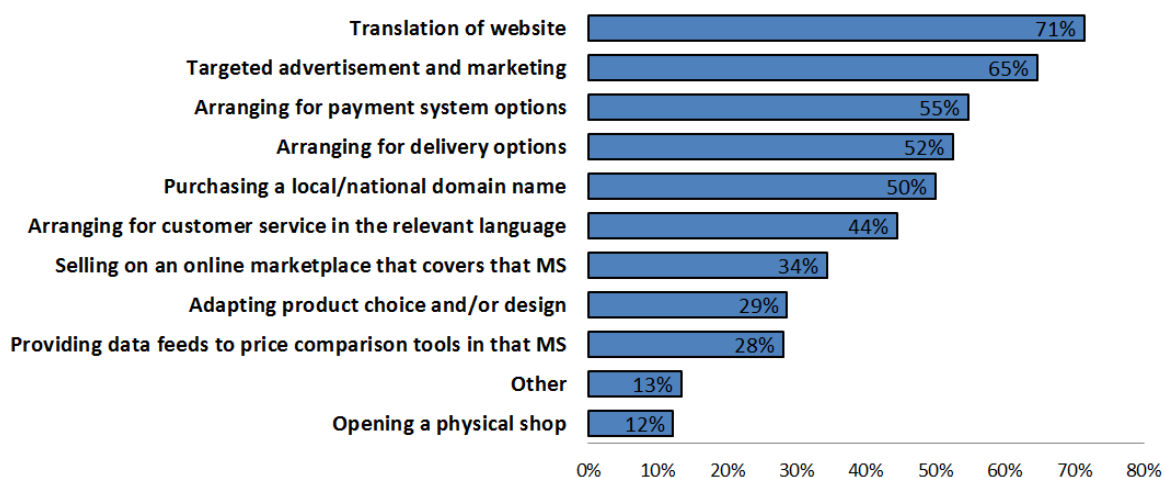
- (354) Product differentiation may help manufacturers and retailers to price differentiate across countries by charging different prices for different versions of the products. This may explain why for consumer electronics price differences for specific products are reported to be rather limited despite the high proportion of product differences that were reported.
- (355) Cross-border sales restrictions, implemented through geo-blocking or geo-filtering could be motivated by suppliers' interests to ensure that different prices are applied in different Member States for the same product. For that to be possible, (potential) customers from the Member States where prices are higher for a specific product must be prevented from buying the product from the Member States where it is cheaper. Geo-filtering and geo-blocking measures may serve to prevent such "arbitrage" opportunities. Overall consumer welfare is expected to decrease if, as a result of the price discrimination and geo-filtering/geo-blocking, total output decreases or remains the same. In case total output would increase, the welfare effect of price discrimination along national borders is a priori ambiguous.²¹⁷ However, in case price discrimination allows the company to serve a market which would otherwise not be served, the effect on overall consumer welfare should normally be positive.

4.3.2.7 Commercial reasons for not selling cross-border and costs of supplying abroad

- (356) Targeting customers cross-border requires specific measures that come at a cost and limited cross-border activities of retailers can partially be explained by the costs/efforts needed to successfully sell in other Member States. The figure below shows the percentage of retailers that either took or would take the predefined measures in order to launch or increase online sales in other Member States, where they were not significantly present or not present at all.

²¹⁷ Whilst removing the possibility to price discriminate by means of geo-blocking or geo-filtering may increase overall consumer welfare, such an increase may, however, involve distribution effects across customers groups, some may benefit from a price decrease, while others may experience a price increase.

Figure B. 52: Proportion of retailers indicating that they took or would take certain steps in order to launch or increase online sales in other Member States²¹⁸



(357) The responses show that retailers consider a significant number of measures to be advisable in order to successfully sell online into a new geographic market.

(358) The measure mentioned by most respondents involves translation of the website, while the second most often indicated one involves targeted advertising and marketing.

(359) The majority of respondents that mention translation of the website as a measure to increase cross-border sales in Member States where they were not (significantly) present have also pointed to other measures. For instance, almost three quarters of the respondents mention targeted advertising or marketing as a measure they have or would take in order to enter or increase sales into a Member State.

(360) Similarly, of the respondents that would translate the website as a measure (a) almost three quarters indicate that they would, in addition, start providing data feeds to price comparison tools in that Member State, (b) three quarters would, in addition, start selling on an online marketplace that covers also that Member State, and (c) 86 % indicate that they, in addition, would purchase a local/national domain name.

(361) Retailers were also asked about the main categories of costs they incur when entering as an online retailer in a new Member State. In addition to costs which are related to the measures described in Figure B. 52 above, companies frequently face costs due to the need for local legal or tax advice as well as the need for specific IT to handle the processing of orders.

(362) The actual costs incurred are case specific and depend on the strategy of the retailer. They can range from a few thousands to several million Euros. Based on the responses by retailers, opening a new dedicated website in another Member State is generally

²¹⁸ Proportions are calculated of the 872 respondents that answered the relevant question. Note that each respondent was able to select several measures.

considered to be more expensive than selling via marketplaces where the additional costs are typically limited to commissions paid to the marketplace.

- (363) Retailers also incur additional costs when serving customers located in a Member State other than the one where the retailer's website is established. Additional costs that were reported typically include higher costs for delivery and return handling as well as higher payment costs related to higher charges by some payment service providers for cross-border transactions or the need to introduce alternative payment systems.
- (364) Often, the decision on whether to sell cross-border or not is a general business decision by a retailer and is not related to contractual or other arrangements with suppliers. Many retailers decide to sell to customers in a certain Member State only and refrain from selling cross-border as it adds additional costs.
- (365) Even if retailers decide to enter a new geographic market, many do so rather by setting-up a dedicated website with a Member State specific URL and support staff in the Member State than by selling cross-border from an established website. Based on the responses received, such newly established websites frequently target only customers from that Member State.

4.3.3 Contractual territorial restrictions to sell and advertise online

- (366) As just explained, there may be a number of reasons and factors why retailers decide not to sell cross-border to customers in other Member States. Unilateral business decisions of non-dominant retailers not to sell cross-border at all or not to sell cross-border to customers in certain EU Member States do normally not raise any concerns under the EU competition rules.
- (367) There are, however, also indications of contractual restrictions²¹⁹ which restrict retailers from selling cross-border to customers outside their home Member State.

4.3.3.1 Agreements between manufacturers and retailers restricting cross-border online sales

- (368) To evaluate the existence of cross-border online sales restrictions, retailers were asked whether they have contractual restrictions limiting their ability to sell cross-border to customers located in a Member State different from where the seller is established. In the 28 EU Member States, almost 12 % of respondents to the retailers' questionnaire report to have such restrictions in at least one product category.
- (369) It is important to note that, since this percentage only indicates the proportion of retailers that have contractual cross-border sales restrictions in at least one product category, it does not allow to draw any conclusions as to how many of their agreements include such restrictions and about the number of products within a certain product category that are affected by such restrictions. While some respondents may only be restricted in relation to one product in one agreement with one supplier, others may

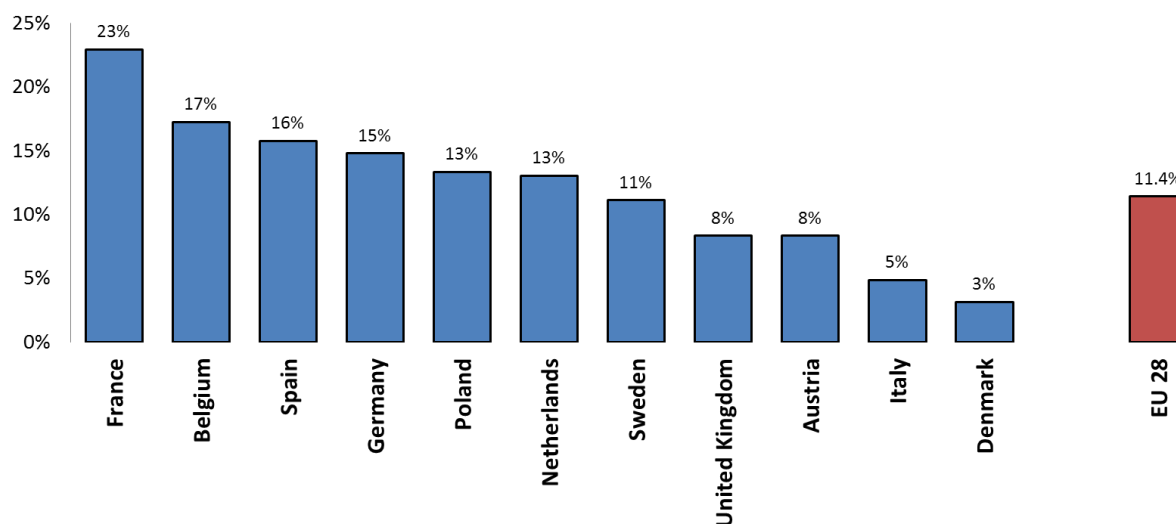
²¹⁹ See paragraph (17).

have territorial restrictions in agreements with multiple suppliers and for multiple products.²²⁰

(370) As regards the relationship between the respondents' size and the presence of contractual territorial restrictions, a higher proportion of retailers with 2014 turnover above EUR 500 000 had contractual cross-border sales restrictions in at least one product category than of retailers with 2014 turnover below EUR 500 000.²²¹ This can be explained among others by the fact that larger retailers frequently sell more products and have more suppliers. The likelihood of cross-border online sales may also be higher for larger retailers than for smaller retailers.

(371) As can be seen from Figure B. 53, the proportion of retailers that have contractual cross-border sales restrictions in at least one product category for each of the Member States varies significantly.

Figure B. 53: Retailers that have contractual restrictions to sell cross-border in at least one product category, by Member State²²²



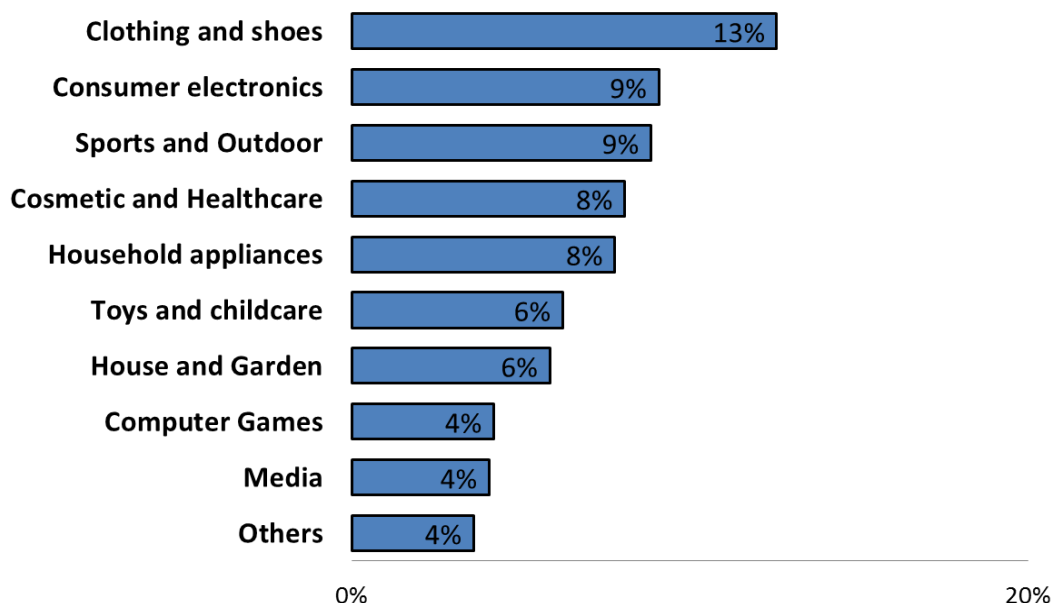
(372) Contractual territorial restrictions were reported in all product categories. The product category with the highest share of contractual territorial restrictions is clothing and shoes followed by consumer electronics and sports and outdoor equipment. The figure below summarizes the proportion of respondents out of all retailers active in a given product category that reported that they have a contractual restriction to sell cross-border for the relevant product category.

²²⁰ Several retailers may have also reported restrictions coming from the same supplier.

²²¹ 13 % of retailers with turnover above EUR 500 000 report having contractual restrictions in at least one product category while 7 % of retailers with turnover below EUR 500 000 report having a contractual restriction in at least one product category. Proportions are calculated out of all respondents that provided information on their turnover (798 for the turnover category above EUR 500 000 and 226 retailers for the turnover category below EUR 500 000).

²²² The proportion at the EU level is taken from all retailers that responded to the retailers' questionnaire. Proportions at the Member State level are calculated out of all retailers that responded from the respective Member State. Only Member States with a minimum of 20 respondent retailers were taken into account.

Figure B. 54: Retailers that have a contractual restriction to sell cross-border for each product category – EU 28²²³



(373) Contractual cross-border sales restrictions appear in multiple forms. The cross-border sales restrictions reported by respondents range from outright bans to sell outside one or more EU Member State to less straightforward restrictions on the ability of retailers to sell their products cross-border. Sometimes the retailer is not explicitly prohibited from selling cross-border, but is obliged to translate its website into the languages of all those Member States into which it is willing to deliver the product. The Commission considers that such a provision may limit any ad-hoc sales cross-border and may increase the costs of selling to customers outside the targeted Member State.

(374) The above mentioned restrictions are not always formulated as prohibitions, but sometimes as requirements, whereby approval by the supplier is needed, before sales into other Member States are permitted. The Commission considers that the impact of such approval requirements may often be the same as an outright prohibition. Only an explicit approval would allow retailers to sell cross-border. Frequently, retailers may not request such an approval and even if they request it a rejection of their request may follow.

(375) Based on the responses of the retailers, cross-border sales restrictions are not only included in written distribution agreements, but also communicated orally. Some retailers report that they have experienced retaliatory measures by manufacturers

²²³ Proportions are calculated out of all respondents that replied to the questionnaire and reported that they are active as retailers in a given product category. Note that a single respondent can be active in several product categories and was therefore able to provide a reply for each product category in which it is active. Therefore, as the basis for the calculation is different, these proportions are not directly comparable to the proportion of respondents (nearly 12 %) that reported that they have contractual cross-border sales restrictions in at least one product category.

including the discontinuation of delivery to them because they sold cross-border or launched a website targeting another Member State than their home Member State.

- (376) Based on observations by some retailers, the contractual restrictions on cross-border sales are sometimes driven by the manufacturer's desire to keep prices in different Member States at a different level. Many manufacturers work with different "recommended price lists" for different Member States. Some respondents reported ad hoc interventions by suppliers to "stabilize" retail prices in certain countries by asking the retailer not to sell products in certain Member States (or raise the price to a certain level) to not negatively affect the price level in this Member State.
- (377) Cross-border sales restrictions can also result from the manufacturer not providing a Union-wide guarantee service under which normally all retailers are obliged to provide the guarantee service and are reimbursed for this service by the manufacturer, even if they were sold by other foreign retailers to customers in their territory.²²⁴
- (378) Approximately 5 % of respondent retailers report that some of the manufacturers indicated that the manufacturer guarantee would not be recognised for products which they sell cross-border.²²⁵ 97 % of the respondent manufacturers indicated that they do not provide different commercial guarantees for cross-border transactions.²²⁶ Furthermore, 99 % of the respondents do not apply different guarantees online and offline unless for regulatory reasons or due to the obligation towards a marketplace that requires longer guarantee periods as an admission criterion.
- (379) Few respondents indicate that they extend or reduce the commercial guarantee in cross-border sales to adapt to local legal requirements of the Member State of the customer. Some manufacturers indicate that local sales points have the commercial autonomy to make promotions on commercial guarantees that apply only within their own territory as long as they do not fall below minimum legal requirements.
- (380) There are also examples of contractual clauses under which manufacturers grant distributors territorial protection by limiting the possibility of other distributors to sell into their territory for a certain period of time in relation to new products which are introduced at different times in various Member States.²²⁷

²²⁴ See Vertical Guidelines, paragraph 50.

²²⁵ Proportion calculated out of 861 retailers that responded to the relevant question.

²²⁶ Proportion calculated out of 247 manufacturers that responded to the relevant question.

²²⁷ See Vertical Guidelines, paragraphs 61 and 108.

4.3.3.2 Monitoring of customer location

(381) The Commission has questioned manufacturers as well as retailers whether they monitor the compliance with contractual territorial restrictions and the reasons for doing so.

(382) 13 % of respondent manufacturers report to either monitor or ask retailers to monitor the location of customers to which retailers sell their products within the EU.²²⁸ Only a small proportion of retailers indicate that they collect information concerning the location of the customer because their manufacturers request them to do so and the majority indicate that they do this based on their own business decision.²²⁹

(383) On the other hand, approximately 22 % of respondent retailers indicate that some of their manufacturers use a system of serial number tracking or an equivalent system to identify the retailer from which a specific product was bought.²³⁰

(384) Manufacturers were asked about the reasons for their monitoring activities. Next to ensuring compliance with territorial sales restrictions (such as active sales restrictions into exclusively allocated territories) the main reasons reported were:

- (a) To be able to understand the market and adopt the right (online) sales and marketing strategies for each Member State,
- (b) To be able to apply existing bonus policies and incentivise retailers appropriately,
- (c) To monitor guarantees and allow the activation of products,
- (d) To ensure the desired after-sales services,
- (e) To prevent unauthorized sales (within selective distribution systems),
- (f) To prevent the sale of counterfeit products.

4.3.3.3 Geo-blocking measures, territorial restrictions and the EU competition rules

(385) In the absence of a dominant market position, the EU competition rules are not concerned with geo-blocking on the basis of unilateral business decisions taken by companies, but only with geo-blocking measures which implement contractual

²²⁸ Proportion calculated out of 248 manufacturers responding to the relevant question.

²²⁹ Approximately 4 % of the 611 retailers that responded to the relevant question indicated that the decision to collect information concerning the location of the customer is partly determined by them and partly determined by their supplier. Only one retailer indicated that it collects such location information solely because of a request by its supplier. The answers of retailers may have been impacted by the fact that all of them need to collect such information for the purposes of delivering and billing the product and that this is the predominant reason for collecting such data.

²³⁰ Proportion calculated out of 859 retailers that responded to the relevant question.

restrictions limiting the ability of online retailers to sell to certain territories or customer groups.²³¹

(386) Geo-blocking measures based on unilateral decisions by non-dominant undertakings²³² fall outside the scope of Article 101 TFEU whereas geo-blocking measures taken on the basis of agreements or concerted practices between distinct undertakings may fall under Article 101 TFEU.

(387) The European Courts have on a number of occasions held that agreements/concerted practices which are aimed at partitioning national markets according to national borders or which make the interpenetration of national markets more difficult, in particular those which are aimed at preventing or restricting parallel exports, have as their object the restriction of competition pursuant to Article 101(1) of the TFEU.²³³

(388) Geo-blocking measures implemented by vertically integrated undertakings that produce goods and sell them through their own websites fall outside the scope of Article 101 TFEU. Equally, if a retailer unilaterally decides not to sell to customers in certain Member States and implements this decision through geo-blocking measures, that decision does not fall under Article 101 TFEU.²³⁴

(389) If geo-blocking measures result from an agreement or concerted practice that is not a genuine agency agreement²³⁵ between two undertakings (such as a manufacturer and a retailer), they may fall within the scope of Article 101(1) TFEU.

(a) Territorial sales restrictions under Article 4(b) of the Vertical Block Exemption Regulation

²³¹ Unilateral conduct may, however, be caught by Article 102 TFEU and/or by Article 20(2) of Directive 2006/123/EC on services in the internal market, which provides that "Member States shall ensure that the general conditions of access to a service, which are made available to the public at large by the provider, do not contain discriminatory provisions relating to the nationality or place of residence of the recipient, but without precluding the possibility of providing for differences in the conditions of access where those differences are directly justified by objective criteria".

²³² Agreements between legal entities within the same undertaking fall outside the scope of Article 101(1) TFEU. See for example judgment in *Centrafarm BV and Adnaan De Peijper v. Sterling Drug Inc*, 15/74, EU:C:1974:114, paragraph 41 and judgment in *Viho Europe BV v. Commission*, C-73/95 P, EU:C:1996:405, paragraph 51.

²³³ See, for example, judgment in *Établissements Consten S.à.R.L. and Grundig-Verkaufs-GmbH v Commission of the European Economic Community*, 56/64 and 58/64, EU:C:1966:41; judgment in *P Commission v GlaxoSmithKline*, C-513/06, EU:C:2008:738, paragraphs 58 to 61; judgment in *Sot.Lélos kai Sia and Others*, C-468/06 to C-478/06, EU:C:2008:504, paragraph 65; judgment in *NV IAZ International Belgium and Others v Commission*, 96 to 102, 104, 105, 108 and 110/82, EU:C:1983:310, paragraphs 23 to 27; judgment in *Javico*, C-306/96, EU:C:1998:173, paragraphs 13 and 14; judgment in *General Motors v Commission*, C-551/03 P, EU:C:2006:229, paragraphs 67 to 69 and judgment in *Football Association Premier League and Others*, C-403/08 and C-429/08, EU:C:2011:631, paragraph 139.

²³⁴ As indicated above, the Commission adopted a proposal on 25 May 2016 (COM(2016) 289 final) to tackle unilateral geo-blocking of companies.

²³⁵ Geo-blocking measures in agreements between undertakings may fall outside Article 101(1) TFEU if the relationship between the parties is qualified as a "genuine" agency relationship within the meaning of the case-law. The decisive element is whether the agent bears financial or commercial risks in relation to the activities for which it has been appointed as an agent to the principal. See judgment in *CEEES*, C-217/05, EU:C:2006:784 paragraphs 51 to 61 and judgment in *CEPSA*, C-279/06, EU:C:2008:485, paragraph 36.

- (390) Article 4(b) of the Vertical Block Exemption Regulation provides that, subject to a number of limited exceptions, the exemption provided for in the Vertical Block Exemption Regulation does not apply to a vertical agreement between a supplier and distributors that directly or indirectly has as its object to restrict the territory into which, or of the customers to whom, the distributor may sell the contract goods.
- (391) Article 4(b) of the Vertical Block Exemption Regulation covers both direct and indirect restrictions (such as reduction of bonus payments or rebates) aimed at inducing distributors not to sell to customers in certain territories.²³⁶
- (392) A supplier can, however, restrict the territory into which or the customers to whom a distributor may sell the goods or services if one of the exceptions listed in Article 4(b)(i) to (iv) of the Vertical Block Exemption Regulation is met.
- (393) In particular, Article 4(b)(i) of the Vertical Block Exemption Regulation provides that a supplier can restrict active sales into the exclusive territory or to an exclusive customer group reserved to the supplier or allocated by the supplier to another distributor. Active sales mean actively approaching individual customers by for instance direct mail, including the sending of unsolicited e-mails, or visits; or actively approaching a specific customer group or customers in a specific territory through advertisement in media, on the internet or other promotions specifically targeted at that customer group or targeted at customers in that territory.²³⁷ Online advertisement which is specifically addressed to customers in certain territories is also considered as a form of active selling (e.g. territory-based banners on third party website or paying a search engine or online advertisement provider to have advertisements displayed in a particular territory²³⁸). Similarly, launching a website which is targeting a specific Member State by using the country-specific top-level domain (e.g. ".it" for Italy) can be considered as actively selling into that territory.
- (394) The reason for the exception in Article 4(b)(i) of the Vertical Block Exemption Regulation is that exclusive territorial distribution can create efficiencies that justify a restriction on active sales. A distributor that has been exclusively allocated a territory may be incentivised to invest in additional promotion and marketing efforts, possibly to enter a new geographic market, on which other distributors could free ride absent any territorial protection.²³⁹
- (395) By contrast, a restriction of passive sales into an exclusively allocated territory falls outside of the scope of Article 4(b)(i) of the Vertical Block Exemption Regulation and

²³⁶ See Vertical Guidelines, paragraph 50, for further examples of such indirect measures.

²³⁷ Advertisement or promotion that is only attractive for the buyer if it (also) reaches a specific group of customers or customers in a specific territory, is considered active selling to that customer group or customers in that territory. See Vertical Guidelines, paragraph 51.

²³⁸ See Vertical Guidelines, paragraph 53.

²³⁹ Restrictions of active sales into certain territories or customer groups which are unrelated to an exclusive territory or an exclusive customer group reserved to the supplier or allocated by the supplier to another buyer constitute a hardcore restriction under Article 4 (b) of the Vertical Block Exemption Regulation.

constitutes a hardcore restriction as this would grant the distributor absolute territorial protection. Passive sales generally mean sales in response to unsolicited requests from individual customers including delivery of goods to such customers. Sales that result from advertising or promotion aimed to customers in one's own territory/in non-exclusive territories but that also reaches customers in other distributors' (exclusive) territories or customer groups are considered passive sales.²⁴⁰

(396) The Vertical Guidelines provide several examples of restrictions that may have as their object to restrict passive sales via the internet and thus may be hardcore restrictions unable to benefit from the exemption provided in the Vertical Block Exemption Regulation.

(397) This includes for example restrictions that require a retailer to apply different geo-blocking measures (such as blocking access to its website to customers located in another Member State or re-routing customers to an alternative website).²⁴¹

(b) Territorial sales restrictions in selective distribution agreements under Article 4(c) of the Vertical Block Exemption Regulation

(398) Article 4(c) of the Vertical Block Exemption Regulation provides that the exemption does not apply to a vertical agreement between a supplier and a retailer that directly or indirectly has as its object to restrict active or passive sales to end users by members of a selective distribution system, without prejudice to the possibility of prohibiting a member of the system from operating out of an unauthorised place of establishment.²⁴²

(399) Retailers in a selective distribution network should, therefore, generally be free to sell to all customers and this freedom can only be restricted to protect an exclusive distribution system operated in another territory.²⁴³

(400) The exemption of the Vertical Block Exemption Regulation does also not apply to restrictions of cross-supplies between distributors within a selective distribution system, including between distributors operating at different level of trade. If a selective distribution system is operated across several Member States, cross-border sales restrictions between authorized distributors would amount to a hardcore restriction under Article 4(d) of the Vertical Block Exemption Regulation.

²⁴⁰ See Vertical Guidelines, paragraph 51.

²⁴¹ Vertical Guidelines, paragraph 52.

²⁴² Article 1(e) of the Vertical Block Exemption Regulation defines "selective distribution systems" as a distribution system where 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 where these distributors undertake not to sell the goods or services to unauthorised distributors within the territory reserved by the supplier to operate the system.

²⁴³ See Vertical Guidelines, paragraph 56.

4.3.3.4 Indications of contractual territorial restrictions

- (401) The preliminary findings of the sector inquiry suggest that a number of territorial restrictions may raise concerns regarding their compatibility with Article 101 TFEU.
- (402) First, there are indications of contractual restrictions limiting retailers' ability to sell to customers outside their Member State of establishment or to customers located in certain Member States.
- (403) Second, certain suppliers appear to restrict active sales by retailers outside a designated territory, irrespective of whether other territories have been exclusively allocated to other retailers or reserved to the supplier.
- (404) Third, certain manufacturers seem to restrict passive sales into territories that have been exclusively allocated to other distributors or reserved for the supplier.
- (405) Fourth, certain suppliers operating a selective distribution system across several Member States appear to limit the ability of authorised retailers to actively and passively sell to all customers within those Member States (in some cases by limiting the ability of the retailers to launch websites targeting other Member States than their home Member State).
- (406) Lastly, a few manufacturers combine the appointment of an exclusive distributor for a certain territory at the wholesale level with a selective distribution system operated across several Member States and limit the ability of the appointed wholesalers to actively sell to all authorized distributors within the Member States in which the selective distribution network is operated.
- (407) The review of the agreements provided by respondents shows that territorial exclusive distribution agreements can only partially explain the existence of restrictions on (active) cross-border sales and many cross-border sales restrictions are unrelated to exclusive distribution agreements.

Summary

Manufacturers active in all product categories tend to sell their products in a large number of Member States, either by selling directly to retailers or by selling to wholesalers.

Geographic sales strategies of retailers vary significantly amongst the respondents.

Across all product categories covered by the sector inquiry, many retailers are limiting their sales efforts to specific Member States and are not selling cross-border. Engaging in targeted sales cross-border comes at a cost and the decision not to sell cross-border is often based on a general business decision of the retailer whether to expand the geographic scope of its activities to other Member States or not.

36 % of respondent retailers reported they do not sell cross-border for at least one of the relevant product categories in which they are active. 38 % of retailers collect information on

the location of the customer in order to implement geo-blocking measures. Retailers with a higher turnover are more likely to apply geo-blocking compared to smaller retailers. Geo-blocking most commonly takes the form of refusal to deliver goods to customers in other Member States, followed by refusals to accept payments from such customers. The majority of geo-blocking measures in relation to goods result from unilateral business decisions of retailers not to sell cross-border.

Marketplaces can facilitate cross-border online sales. They are particularly relevant for smaller and medium-sized retailers which report to generate on average the majority of their cross-border sales via marketplaces. Marketplaces are of less relevance for large online retailers which typically realize the majority of their cross-border sales on their own websites.

Approximately three quarters of respondent retailers which sell cross-border indicated that they do not charge different prices when selling cross-border to customers in another Member State.

Almost 12 % of retailers indicate that they have contractual cross-border sales restrictions in at least one product category in which they are active.

A higher proportion of the larger retailers (in terms of turnover) experience cross-border sales restrictions compared to smaller retailers. The product category in which the highest proportion of retailers experiences cross-border sales restrictions is clothing and shoes with 13 %, followed by consumer electronics and sports and outdoor.

Contractual cross-border sales restrictions have multiple forms and are not always written in agreements, but are sometimes communicated orally.

The preliminary findings of the sector inquiry suggest that a number of territorial restrictions may raise concerns regarding their compatibility with EU competition rules.

4.4 Restrictions to sell on online marketplaces

(408) As described earlier, different marketplaces with varying business models have emerged in the last 15 to 20 years allowing independent sellers and buyers to sell and purchase products online on their platform.²⁴⁴

(409) Marketplaces have become an important sales channel for many online retailers as well as manufacturers as they can provide them with access to a large number of customers which are looking for products on the respective marketplace. Marketplaces may allow starting an online sales business with lower initial investments. They may also facilitate cross-border sales.²⁴⁵ On the other hand, some manufacturers are critical of marketplaces mainly because of brand image considerations.

²⁴⁴ See section B.1.3 Marketplaces on characteristics of respondent marketplaces.

²⁴⁵ About a third of the retailers that responded to the questionnaire have indicated "selling through a marketplace" as one possible way to increase online sales in Member States where they either do not sell at all or do not sell significant quantities.

(410) The question to which extent contractual restrictions that preclude retailers from selling via online marketplaces (so-called marketplace or platform bans) may raise concerns under the EU competition rules has attracted significant attention in the past years in some Member States.

(411) One of the aims of the sector inquiry is to better understand the prevalence and characteristics of marketplace restrictions and the importance of marketplaces as a sales channel for retailers and manufacturers. In order to gather relevant data, retailers, marketplaces as well as manufacturers were questioned about the use of marketplaces and contractual restrictions limiting the ability of retailers to sell on marketplaces.

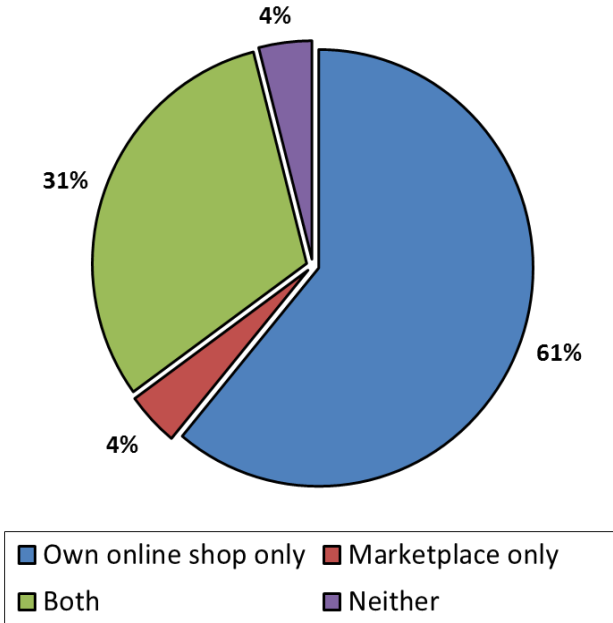
(412) The following section analyses the importance of marketplace sales as a sales channel for retailers and the impact that marketplace sales may have on the business of manufacturers. This will be followed by an analysis of contractual restrictions to sell on marketplaces encountered in the sector inquiry.

4.4.1 Importance of marketplaces as a sales channel for retailers

(413) To determine the importance of marketplaces as an online sales channel, the Commission has questioned retailers as well as marketplaces about their sales activities.

(414) As shown in Figure B. 55 below, more than 90 % of respondent retailers use their own online shop when selling online. 61 % of respondent retailers use their online shops as the sole online selling channel, whereas 31 % of respondent retailers sell via their online shops as well as on marketplaces. 4 % of the respondent retailers sell online only via marketplaces.²⁴⁶

Figure B. 55: Proportion of retailers using different sales channels for selling online

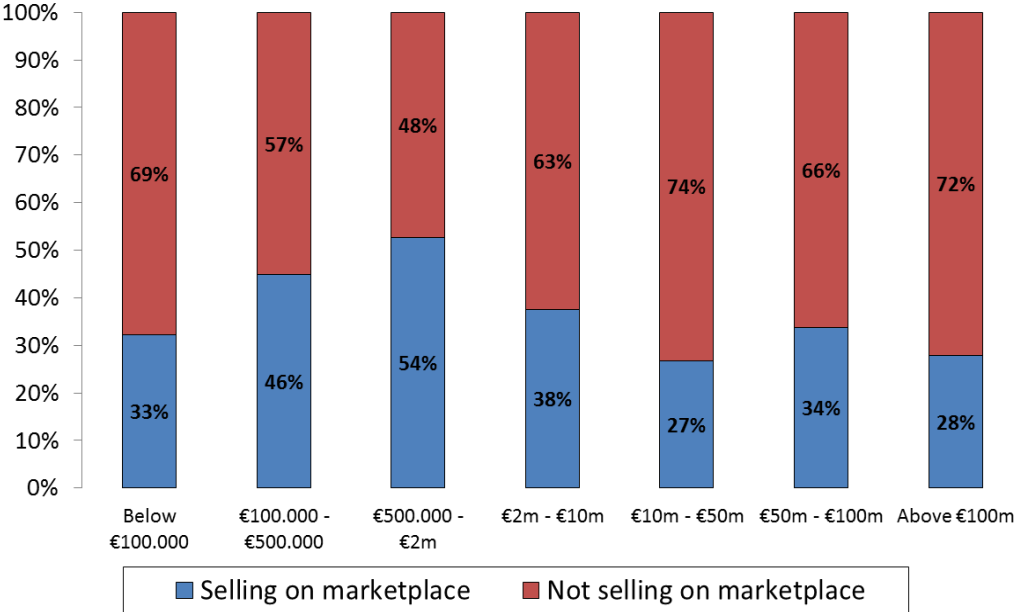


²⁴⁶ Proportions are calculated out of all retailers who responded to the relevant questions, namely 1009.

(415) The average conversion rate, that is, the proportion of website visits which result in a purchase, on retailers' own website tends to be slightly lower (4 %) ²⁴⁷ than the conversion rates achieved on marketplaces (5 %). ²⁴⁸

(416) Generally, the use of marketplaces as a sales channel is not related to the size of the retailer in terms of its turnover (see Figure B. 56).

Figure B. 56: Proportion of retailers in each turnover category that sell on marketplaces ²⁴⁹



(417) However, when focusing on the different turnover categories, it can be observed that the proportion of retailers that sell via their own online shop only and do not use marketplaces tends to be higher within the larger turnover bands, whereas the proportion of retailers that sell via marketplaces only and do not have their own websites tends to be higher within the smaller turnover bands (see Figure B. 57 and Figure B. 58 below).

²⁴⁷ Figure calculated based on all the retailers who provided the relevant data, namely 663.

²⁴⁸ Figure calculated based on the data of 295 sellers on which marketplaces submitted information.

²⁴⁹ Proportions are calculated out of all respondents in a given turnover category (on the basis of 2014 turnover) who responded to the relevant questions. This number ranges from 74 respondents in the turnover category EUR 50 million to EUR 100 million to 297 respondents in the turnover category above EUR 100 million.

Figure B. 57: Proportion of retailers in each turnover category that sell through own online shop only²⁵⁰

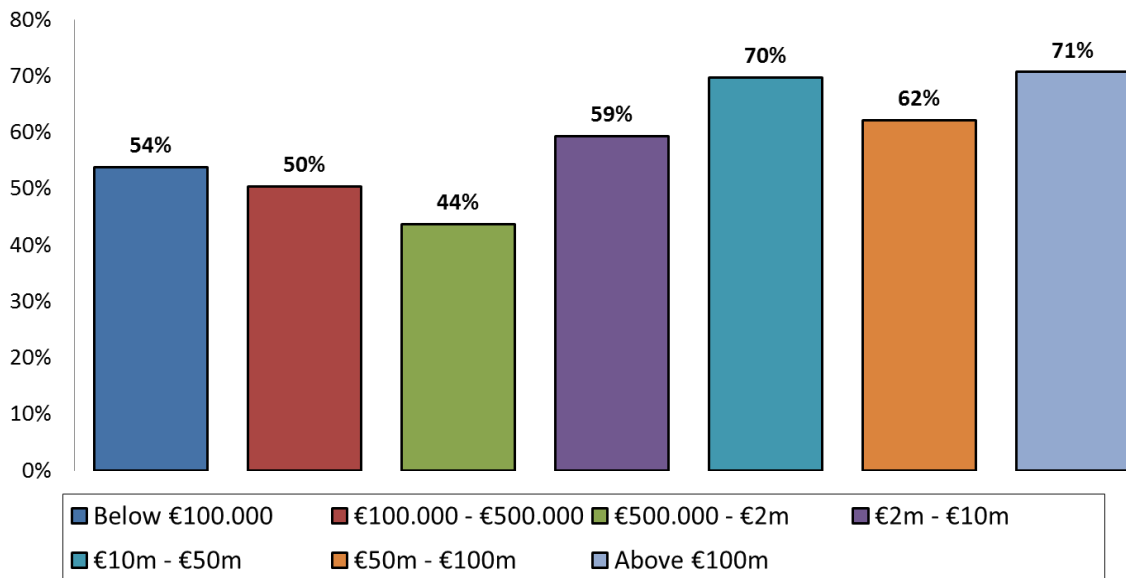
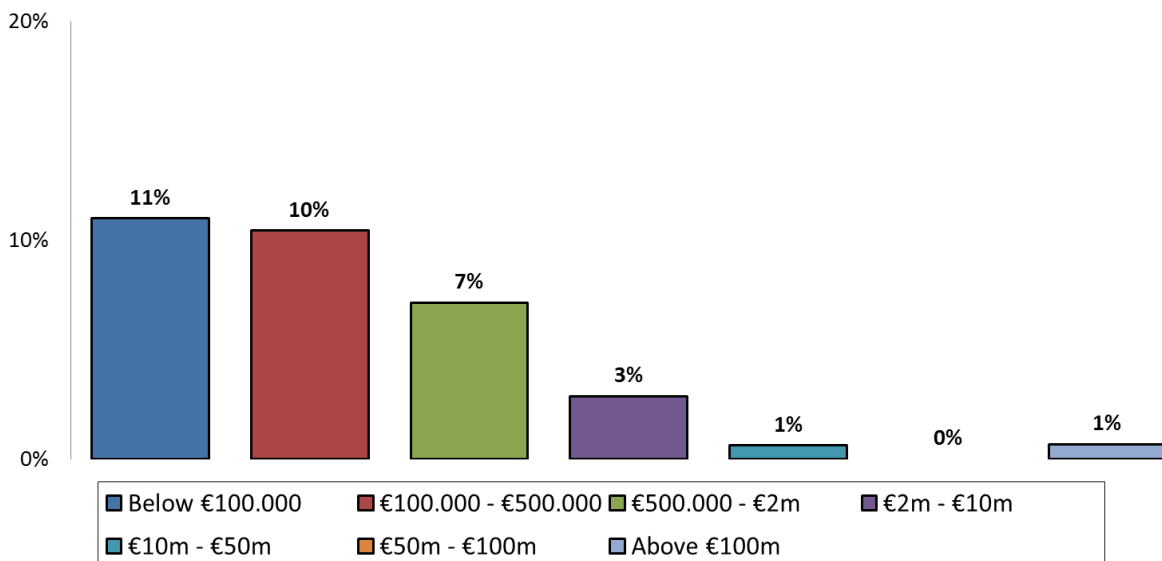


Figure B. 58: Proportion of retailers in each turnover category that sell on marketplaces only²⁵¹

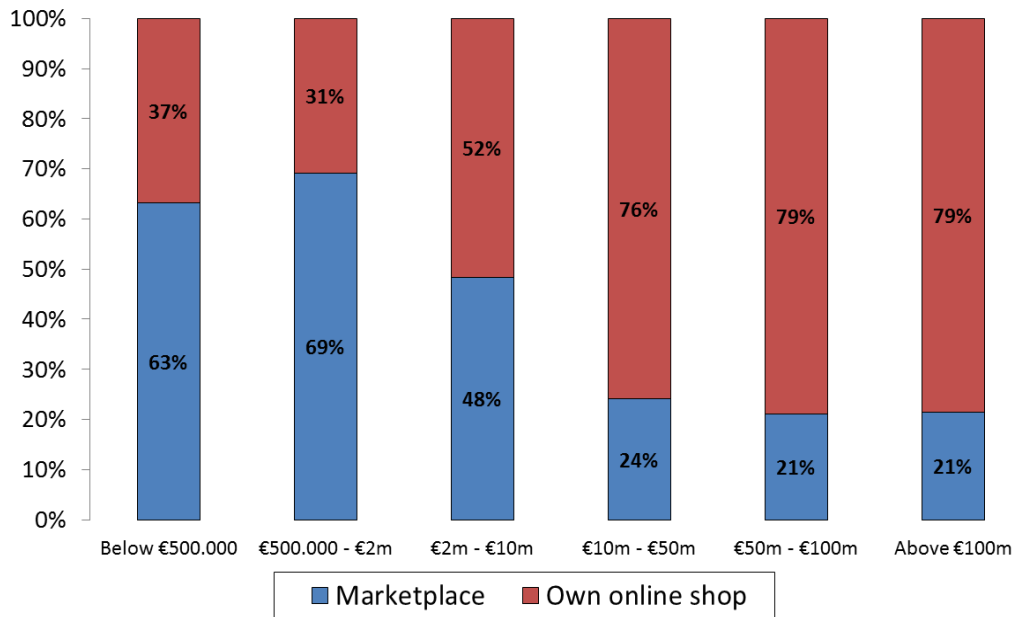


(418) For those retailers that use both own online shops as well as marketplaces for selling goods online, Figure B. 59 shows the proportion of purchases carried out via each of these channels. According to the preliminary finding, smaller retailers tend to realise a larger proportion of their sales via marketplaces than the larger retailers.

²⁵⁰ Proportions are calculated out of all respondents in a given turnover category (on the basis of 2014 turnover) who responded to the relevant questions. This number ranges from 74 respondents in the turnover category EUR 50 million to EUR 100 million to 297 respondents in the turnover category above EUR 100 million.

²⁵¹ Proportions are calculated out of all respondents in a given turnover category (on the basis of 2014 turnover) who responded to the relevant questions. This number ranges from 74 respondents in the turnover category EUR 50 million to EUR 100 million to 297 respondents in the turnover category above EUR 100 million.

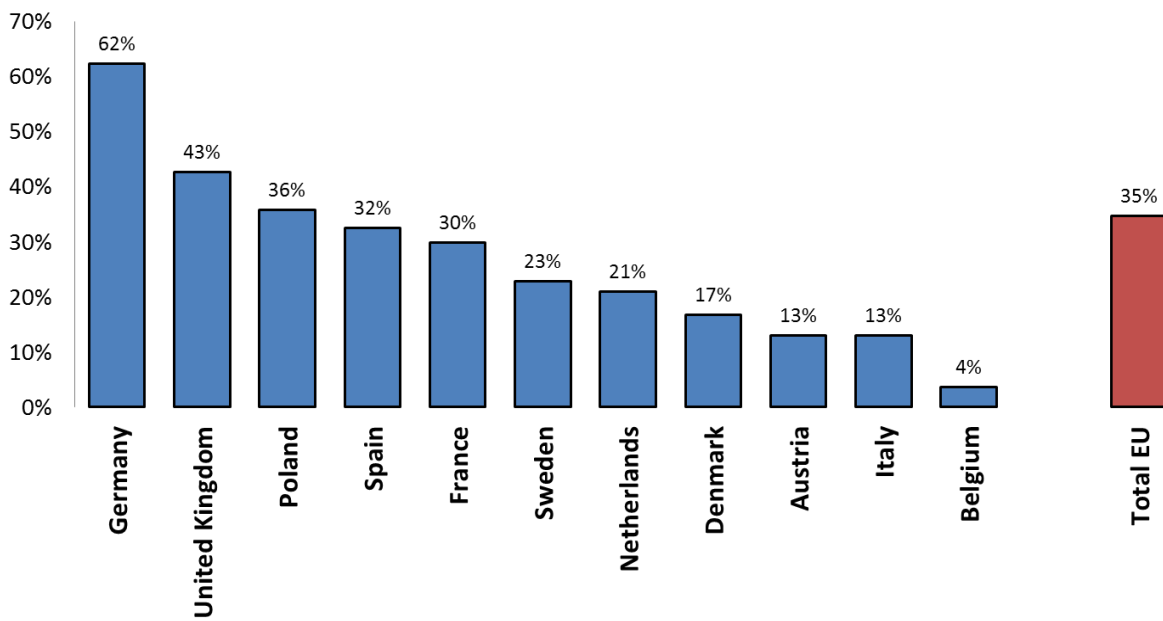
Figure B. 59: Proportion of purchases carried out via marketplaces and own online shops for retailers using both channels in each turnover category²⁵²



(419) There are significant differences in the proportion of retailers that use marketplaces across EU Member States (see Figure B. 60 below).

²⁵² Proportions are calculated out of the total number of purchases reported by respondents in a given turnover category (on the basis of 2014 turnover) who sold both via their own online shop as well as via marketplaces and that provided the relevant information on purchases. The number of respondents ranges from 20 respondents in the turnover category EUR 50 million to EUR 100 million to 40 respondents in the turnover category above EUR 100 million.

Figure B. 60: Proportion of retailers in each Member State that use marketplaces²⁵³

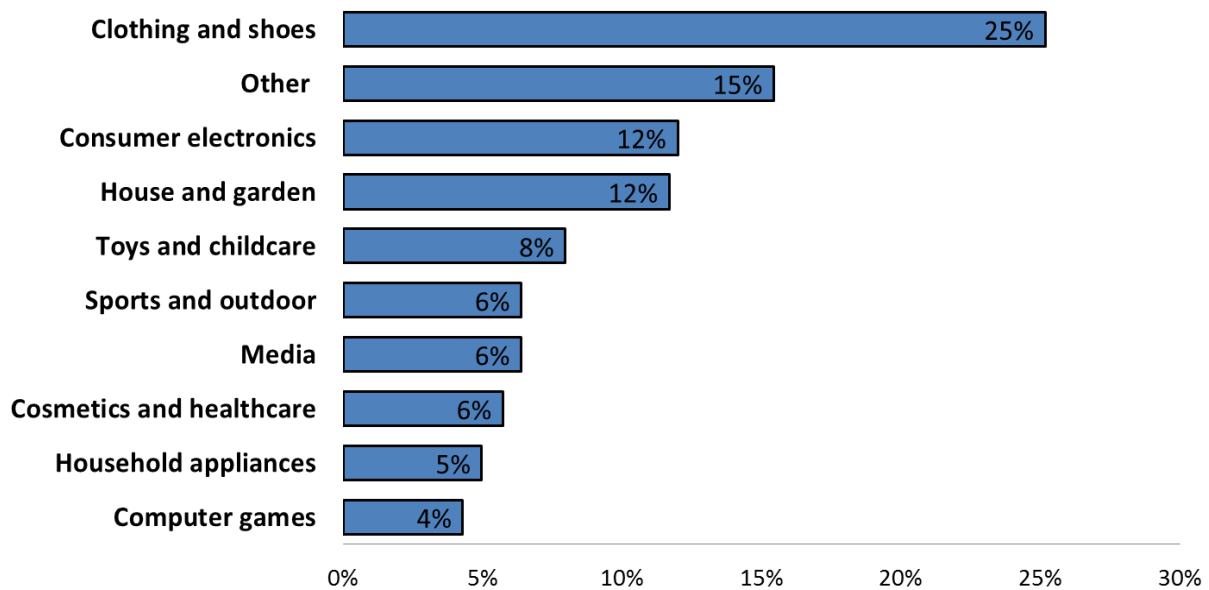


(420) These figures are confirmed by the information provided by the marketplaces. Out of all professional sellers that listed products on one of the marketplaces in the sample in 2014, 85 % were established in United Kingdom, Germany or Poland. Sellers from the remaining Member States account together for only 15 % of all sellers that listed products on these marketplaces in 2014.

(421) Although marketplaces tend to offer a wide variety of product categories, the proportion of professional sellers on the marketplace varies depending on the product category in question (see Figure B. 61).

²⁵³ The proportion at the EU level is calculated out of all retailers who replied to the relevant questions, namely 1009. Proportions at the Member State level are calculated out of all retailers that responded from the respective Member State to the relevant questions. Only Member States with a minimum of 20 respondent retailers were taken into account.

Figure B. 61: Average proportion of professional sellers on marketplaces per product category²⁵⁴



(422) Based on the information provided by marketplaces, the majority of professional sellers that sold via marketplaces in 2014 generated a turnover lower or equal to EUR 50 000 irrespective of the Member State in which they were established.²⁵⁵

(423) Although the average number of professional sellers selling via the respondents' marketplaces was just below 28 000 sellers in 2014, the median number of sellers was just below 2 000. In other words, half of the marketplaces in the sample had less than 2 000 professional sellers selling via their platform whereas half of the marketplaces had more than 2 000 professional sellers. This means that the marketplaces vary considerably in terms of the number of professional sellers selling via their platform. For the marketplaces which were active since at least 2012, the average increase in the number of professional sellers between 2012 and 2014 was 47 % (the median increase for the same period was 26 %) which indicates a growing importance of marketplaces as a sales channel for retailers.²⁵⁶

(424) All in all, the preliminary findings show that marketplaces are an important sales channel especially for smaller and medium-sized retailers. For some of them, marketplaces are the only sales channel whereas some others conclude the majority of their online transactions using this sales channel. The importance of marketplaces is especially apparent in some Member States such as Germany and the United Kingdom. The overall use of marketplaces seems to be increasing over time.

²⁵⁴ Proportions per product category were calculated for each of the 34 marketplaces who replied to the relevant question. Subsequently, the average of these proportions was taken for each product category. The figure shows, for example that professional sellers selling clothing and shoes on a marketplace account on average for 25 % of all sellers on a marketplace.

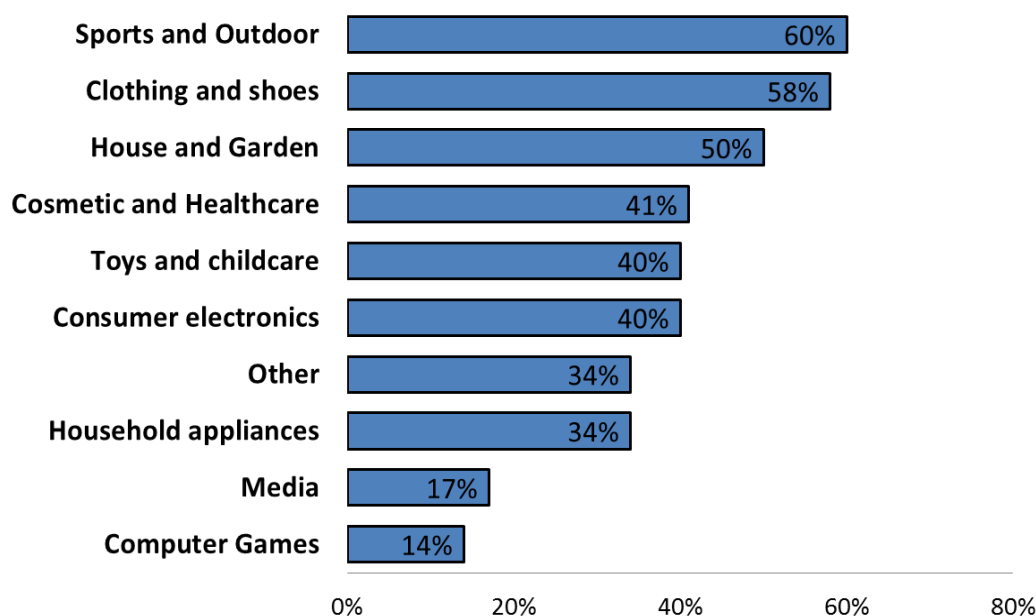
²⁵⁵ This proportion amounts to 89 % for the EU as a whole. Proportion calculated based on the responses of all 37 marketplaces.

²⁵⁶ Figures are calculated based on the responses of all 37 marketplaces.

4.4.2 Impact of sales through marketplaces on the business of manufacturers

(425) Manufacturers were asked whether they consider sales via (certain) marketplaces as having a potentially adverse impact on their business. 48 % of manufacturers indicated that they consider that selling on marketplaces could have a potential adverse impact on their businesses. The proportion of manufacturers that considered marketplaces as a sales channel with a potentially adverse impact is particularly high in the product categories sports and outdoor equipment followed by clothing shoes and accessories as can be seen from the following Figure B. 62.²⁵⁷

Figure B. 62: Proportion of manufacturers in each product category that consider (certain) marketplaces as potentially having an adverse impact²⁵⁸



(426) Some manufacturers point out that the various sales channels including marketplaces can have both a potentially adverse and beneficial impact on their businesses.²⁵⁹ This depends on the particular features of the marketplace such as whether the products are presented in an attractive way, whether the identity of their brands is respected, and whether customers are sufficiently informed about characteristics, features and quality of the products in order to allow them to take an informed buying decision. Should this be the case, marketplaces can – according to these manufacturers – enhance online sales without negatively affecting the brand image.

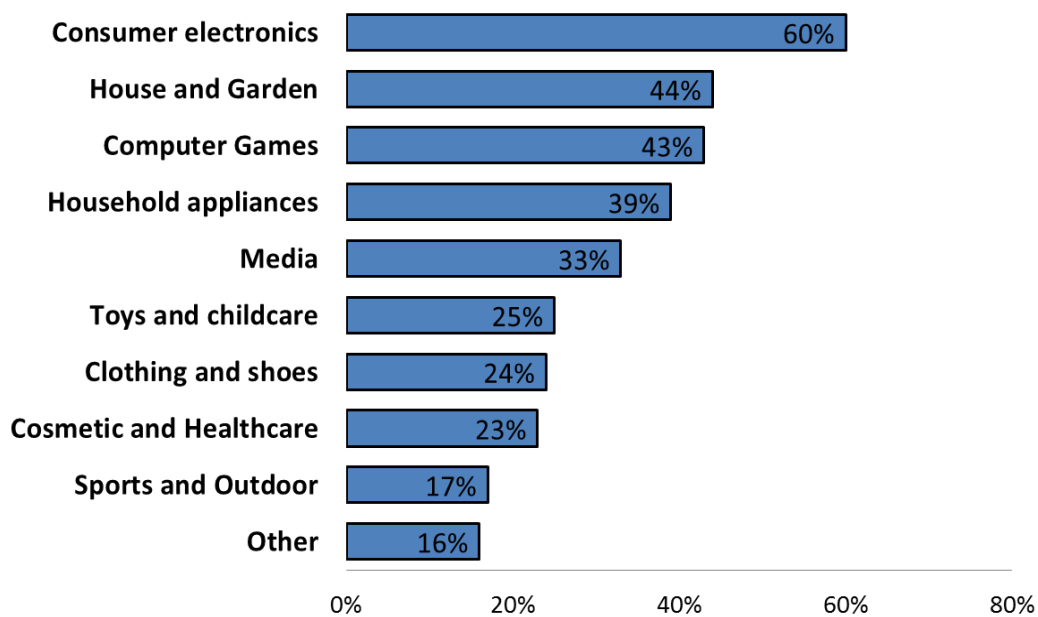
²⁵⁷ These product categories are also the product categories in which most marketplace restrictions can be observed (see Figure B. 67).

²⁵⁸ Proportion calculated out of all suppliers active in the given product category. Note that in the product categories Media and Computer games there are only, respectively, 6 and 7 respondents.

²⁵⁹ This is also evident from the fact that a quarter of the manufacturers who indicate that selling on (certain) marketplaces could have a potentially adverse impact on their business, consider that selling on (certain) marketplaces could also have a potentially beneficial impact on their business.

(427) 19 % of respondent manufacturers are using marketplaces to sell products directly to customers and many manufacturers have stated that they consider that sales via (certain) marketplaces can be beneficial to their business. According to the manufacturers, marketplaces provide high visibility of the products and the brands and enable retailers to reach more customers with low advertising costs. Marketplaces also allow the purchase of the products at any time of the day and from almost any location. In particular manufacturers active in consumer electronics frequently consider marketplaces as beneficial for their business as can be seen from Figure B. 63.

Figure B. 63: Proportion of manufacturers in each product category that consider (certain) marketplaces as potentially having a beneficial impact²⁶⁰



4.4.3 Prevalence and characteristics of marketplace restrictions

(428) There are two main reasons for the choice of retailers not to use marketplaces for their online sales – a unilateral business decision by the retailer and restrictions imposed on the retailer by manufacturers. The following analysis focuses on the latter.

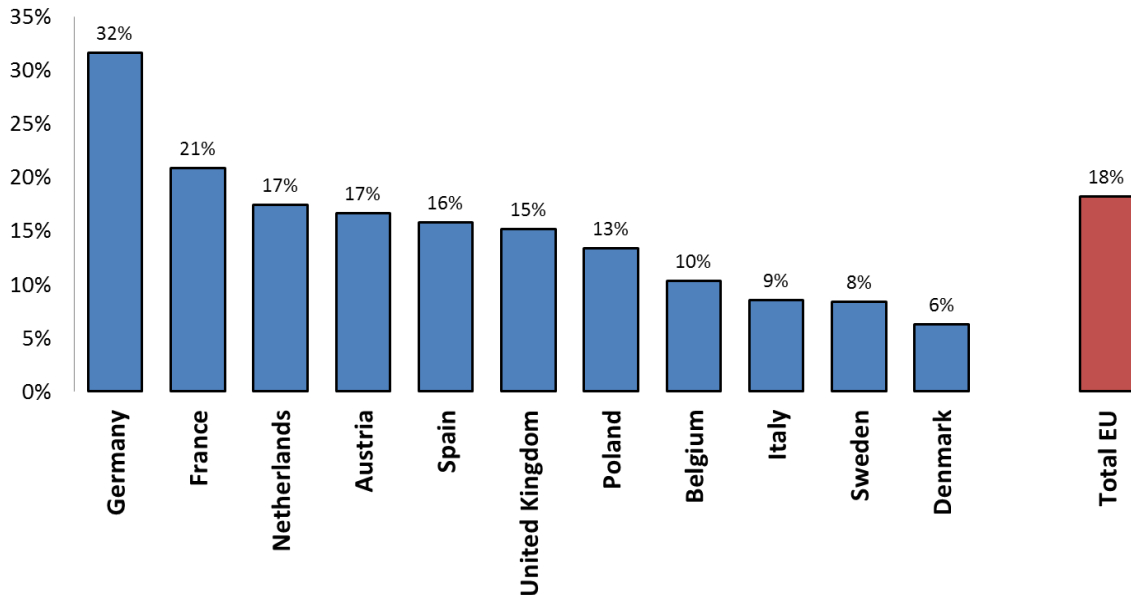
(429) 18 % of retailers that responded to the retailers' questionnaire reported that they have provisions in their agreements with manufacturers or other obligations implemented by indirect means that limit their ability to sell products on one or more marketplaces.

(430) As can be seen from Figure B. 64, the proportion of retailers that have provisions in their agreements with manufacturers or other obligations implemented by indirect means that limit their ability to sell products on one or more marketplaces differs significantly between Member States. The highest proportion of retailers that reported having in place agreements containing some form of marketplace restriction is in

²⁶⁰ Proportion calculated out of all manufacturers active in the relevant product category. Note that in the product categories Media and Computer games there are only, respectively, 6 and 7 respondents.

Germany followed by France, whereas retailers active in other Member States such as Belgium or Denmark rarely report to have marketplace restrictions. These preliminary findings show that marketplace restrictions tend to be more often used in Member States in which marketplaces have established themselves as an important sales channel.

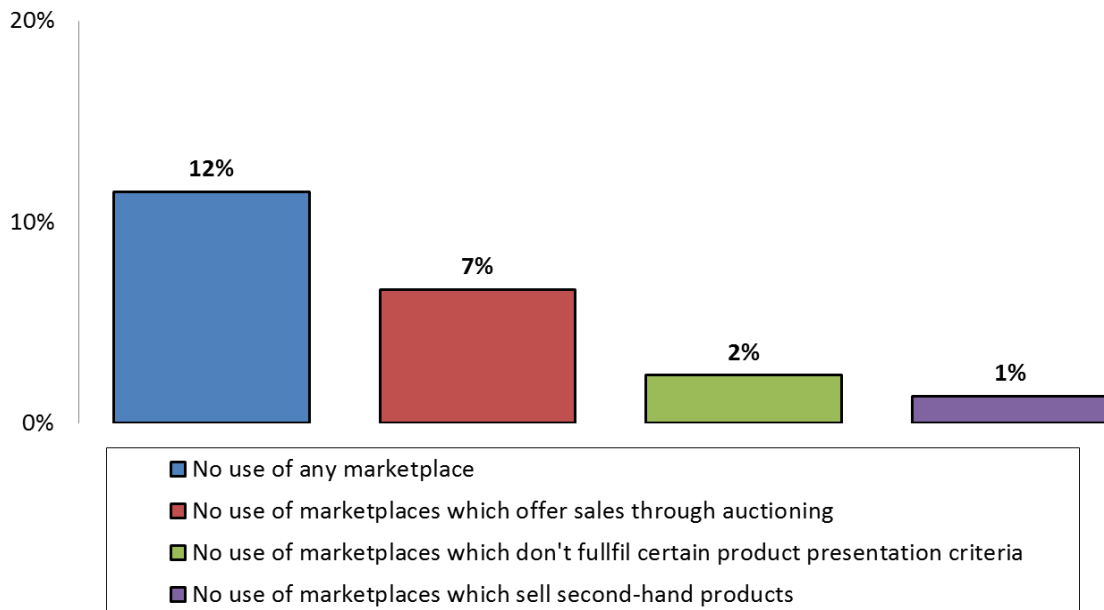
Figure B. 64: Proportion of retailers in each Member State that have agreements containing marketplace restrictions²⁶¹



(431) The responses of retailers also indicate that the types of restrictions regarding sales via marketplaces which retailers encounter differ to a large extent. They range from absolute bans to restrictions of selling on marketplaces that do not fulfil certain quality criteria. Some manufacturers allow sales only on marketplaces that do not offer sales through auctioning. See Figure B. 65 for more details.

²⁶¹ The proportion at the EU level is taken from all retailers that responded to the retailers' questionnaire. Proportions at the Member State level are calculated out of all retailers that responded from the respective Member State. Only Member States with a minimum of 20 respondent retailers were taken into account.

Figure B. 65: Proportion of retailers that have agreements containing different types of marketplace restrictions²⁶²



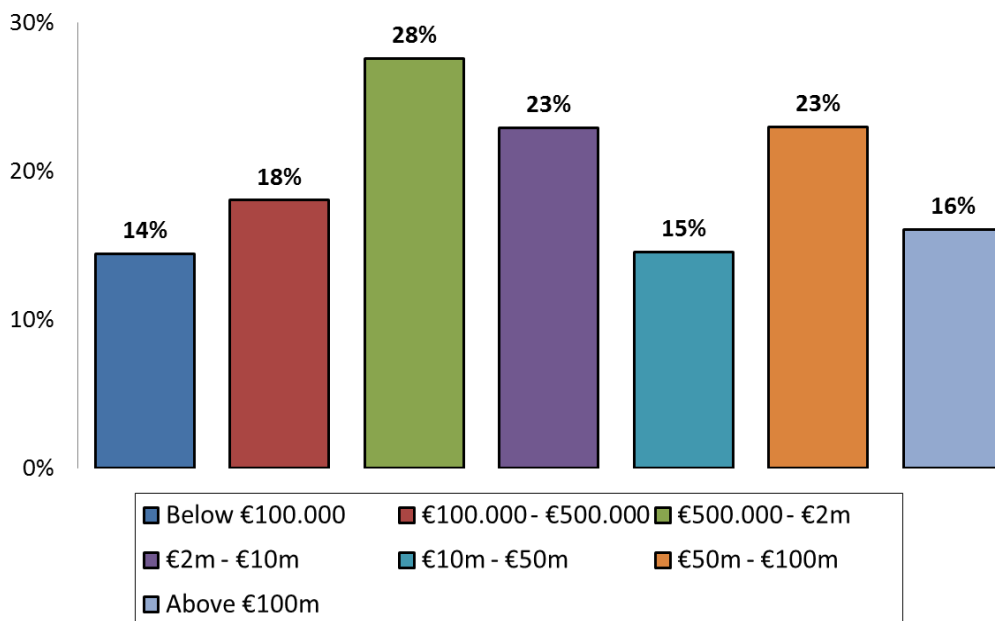
- (432) The preliminary findings show that not only absolute marketplace bans may make it impossible for retailers to sell via all or most of the existing marketplaces.
- (433) Qualitative criteria may have the same impact on retailers as an absolute marketplace ban, if they de facto exclude marketplace sales by requiring compliance with conditions which no marketplace does effectively meet. This may, for example, be the case, if the retailer's website has to appear under a domain name which contains the name of the retailer's business, if the website on which products are sold has to be operated by the retailer or in case of a prohibition to sell via marketplaces that have their logo visible.
- (434) Restrictions allowing sales of products only on specialised marketplaces may in certain circumstances also exclude existing marketplaces as a sales channel for retailers. Whether a specific restriction excludes sales via all or most marketplaces can only be determined on a case-by-case basis.
- (435) Some manufacturers require specific approval for any marketplace via which the retailer intends to sell their products. The Commission considers that the result of such approval requirements may be the same as an explicit prohibition to sell via marketplaces. Retailers may not request such an approval and even if they request it a rejection of their request may follow.
- (436) Restrictions to sell on marketplaces are mostly found in selective distribution agreements. They typically concern branded goods, but they are not limited to luxury products or complex or technical consumer products. Some manufacturers operate

²⁶² Proportions are calculated out of all 1051 retailers that responded to the questionnaire. Please note that each retailer was able to select several types of restrictions on the use of marketplaces.

selective distribution systems (including marketplace restrictions) only in relation to a subset of their products (typically high-end/premium products) and not for their whole product portfolio.

(437) The Commission has analysed whether small and medium-sized retailers are more likely to have agreements containing marketplace restrictions compared to larger retailers. As can be seen from Figure B. 66, according to the preliminary findings there is no correlation between the size of the retailer and the presence of marketplace restrictions in the retailer's distribution agreements. This may be explained by the fact that the terms of selective distribution agreements normally do not differentiate between smaller and larger retailers. However, several retailers claim that some manufacturers use marketplace bans in a discriminatory manner by including them in the agreements with smaller retailers and not including them in the agreements with certain larger retailers.

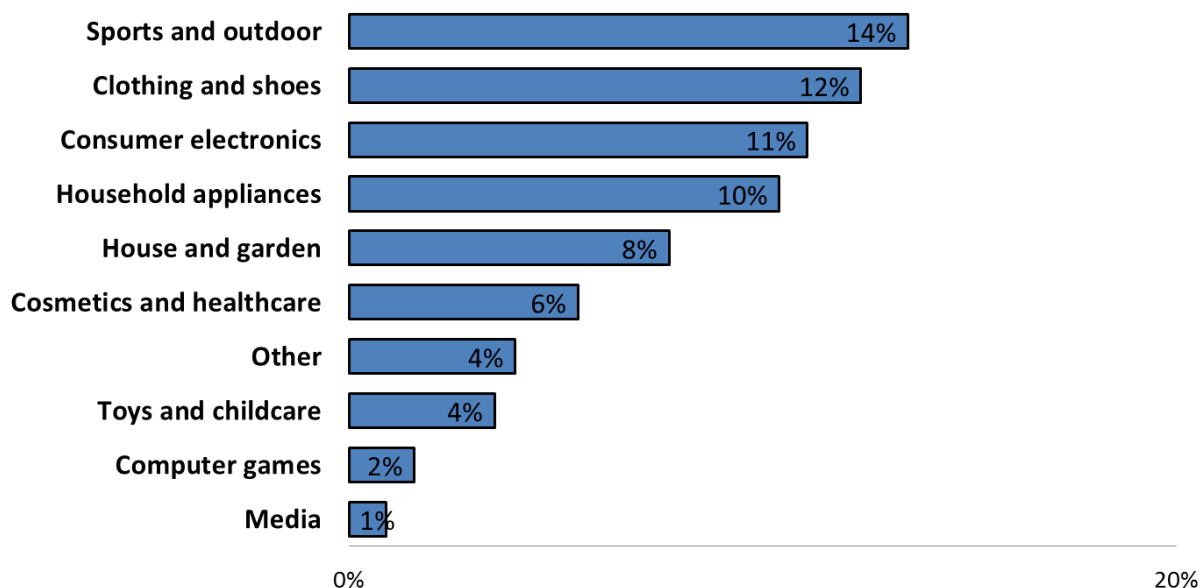
Figure B. 66: Proportion of retailers in each turnover category that have agreements containing marketplace restrictions²⁶³



(438) There are however significant differences between product categories when it comes to the prevalence of marketplace restrictions. As shown in Figure B. 67, retailers selling sports and outdoor equipment or clothing and shoes are more likely to have agreements with restrictions to sell on marketplaces whereas retailers selling media or computer games and software rarely have such agreements in place.

²⁶³ Proportions are calculated out of all retailers in a given turnover category.

Figure B. 67: Proportion of retailers in each product category that have agreements containing marketplace restrictions²⁶⁴



(439) Interestingly, 88 % of the 669 respondent retailers that did not sell on marketplaces in 2014 have not pointed to any restrictions regarding their ability to sell or advertise on marketplaces. This indicates that the decision not to sell via marketplaces is most of the time based on other business considerations and not because retailers are limited in their ability to do so by manufacturers.

(440) Approximately half of the marketplaces that responded to the relevant questionnaire indicated that they are aware of many restrictions on the ability of retailers to sell through marketplaces. 32 % of marketplaces reported that they are aware of some restrictions while 16 % of marketplaces reported that they are not aware of any such restrictions.

(441) Moreover, information provided during the sector inquiry shows that some manufacturers, whose agreements with retailers contain absolute marketplace bans, are either themselves listing their products directly for sale on certain marketplaces or are selling their products to the marketplace operator as a retailer for further re-sale.

4.4.4 Reasons put forward for marketplace restrictions by manufacturers

(442) Manufacturers were given the opportunity to explain why they consider sales via all or some marketplaces as potentially harmful for their business. Marketplaces as well as retailers were also questioned about potential reasons for restrictions on sales via marketplaces.

²⁶⁴ Proportion calculated out of all retailers active in the given product category.

(443) A number of reasons to restrict sales via all or some of the marketplaces have predominantly been put forward by manufacturers or been reported by retailers as the reason put forward by manufacturers. These are as follows:

(a) Protection of the image and positioning of the brand

(444) Some brand owners argue that they spend substantial amounts of money and time to build certain brands and their reputation and that sales via certain marketplaces can have a detrimental impact on these brands. If customers can buy these brands in an environment that is not considered suitable and in which customer expectations in terms of product information, services, advice and ability to experience the products are not met, then this may diminish the value of the brand. The required high level of quality of the selling environment does not only ensure that the customer gets the product that he or she wants, but also allows the customer to understand the key features of the products as well as key differences compared to other products/brands. Products which are sold without meeting the customer expectation will trigger complaints and dissatisfaction and negatively impact the reputation of the products and brands.

(445) Presenting the products on a non-specialized marketplace alongside products of a lesser quality or alongside used or defect products is often considered harmful for the brand image. In particular, owners of luxurious brands have concerns that the presentation on marketplaces in a non-luxury environment without personalized advice and a luxurious shopping experience does not reflect the brand's reputation and therefore diminishes the brand image.²⁶⁵

(446) Moreover, marketplaces are often considered to be too rigid in the way the content and information is presented to the customer. Many brands want to present to their customers a special image (including by means of pictures, text and potentially videos) which is sometimes considered as not sufficiently possible on marketplaces.

(b) Combating the sale of counterfeit products

(447) A large number of manufacturers consider counterfeit products being sold on marketplaces as a serious problem, which is in their view frequently not sufficiently addressed by marketplace operators.²⁶⁶ According to some respondents, marketplaces usually spare the costs of protecting consumers and intellectual right holders against illicit products and try to avoid liability by denying the existence and the extent of counterfeit sales on the marketplace. Moreover, marketplaces earn commissions even

²⁶⁵ Most marketplaces do not differentiate in terms of product presentation between luxurious products and everyday consumer goods.

²⁶⁶ Some retailers consider that brand owners misuse existing notification systems and complain to marketplace operators about sales of products on the marketplace which are allegedly counterfeit products although they are in fact authentic. In these cases, brand owners require marketplaces to de-list the products and request from the retailers to stop selling them. According to the retailers, it often does not help them that they can prove the authenticity of the products. They will ultimately stop selling the products out of fear that their marketplace accounts would otherwise be blocked due to the intervention of the brand owner.

for the sale of counterfeit products which, according to some manufacturers, reduces their incentives to effectively combat counterfeit sales on the marketplace.

(448) The presentation of authentic products alongside counterfeit products is considered to be detrimental for the brand image and some manufacturers consider the level of control over sales on the marketplace as insufficient to address this issue adequately.

(c) Ensuring sufficient pre-and post-sale services

(449) Some manufacturers argue that it is difficult to ensure that sufficient pre-and post-sale services are provided by retailers selling on marketplaces. They argue that marketplaces leave few opportunities for retailers to differentiate between the service level and quality offered. Selling on marketplaces is often purely focused on the price of the products disregarding the features of the different products in terms of quality, design and innovation, all of which are important for the products concerned. If innovative products with new features are not presented and explained adequately, customers may not appreciate the value of the products and turn to products of lower quality.

(450) Moreover, ensuring a high level of advice is considered crucial by manufacturers for certain products for which improper handling or use can create safety and security risks.

(d) Protection of existing distribution channels and brick and mortar shops/free-riding

(451) A number of manufacturers put forward that sales via marketplaces allow retailers which provide little or no pre- or post-sale services to free-ride on investments made by brick and mortar shops that provide customers the possibility to examine and experience the products, but have to invest in specific facilities and human resources to be able to do so. This view was shared by some retailers operating brick and mortar shops.

(e) Concerns about the market position of certain marketplaces and the lack of relationship with customers

(452) Some manufacturers have concerns about the market position of certain marketplaces that may already enjoy a strong bargaining position.

(453) Moreover, some marketplaces impose restrictions on the ability of the retailers to prominently present themselves on the marketplace and establish a direct relationship with the customer. Marketplace sales may therefore not help the retailers to establish a long-term customer relationship with future sale opportunities.

4.4.5 Reasons for marketplace restrictions reported mainly by retailers and some marketplaces

(454) Many retailers as well as marketplaces argue that the main reason for introducing marketplace restrictions is the desire of manufacturers to reduce the number of sellers selling online and to avoid increased price transparency and increased price competition.

(455) Marketplaces allow buyers to easily compare prices across a number of sellers on the marketplace and purchase the products at the lowest price. Marketplace bans may allow manufacturers to stabilize retail prices and reduce competitive pressure on prices. Marketplace bans may therefore not only be in the interest of traditional brick and mortar retailers, but also of manufacturers that operate their own online shop or sell directly via marketplaces to customers.

4.4.6 Possibilities offered by marketplaces to address quality requirements

(456) Many marketplaces invest in order to improve their offering, ensure a high-quality shopping environment and address requests of manufacturers or retailers concerning quality of the content presentation. 86 % of respondents to the marketplace questionnaire indicated that they have taken steps in the last few years to increase the quality and image of their marketplace and related services.

(457) Some marketplaces offer sellers the ability to design their own seller shop within a special area of the marketplace which can reflect the look and feel of a brand or to have specific "showrooms" dedicated to certain brands and designed in line with the suggestions of the brands.

(458) Some marketplaces also run programs which allow them to keep track which sellers are authorized sellers within a selective distribution system of a manufacturer in order to only allow sales via sellers which have been approved and which qualify for the selection criteria applied by manufacturers.

4.4.7. Notice and take down procedures on marketplaces

(459) The Commission questioned marketplaces about the procedures they have in place to allow third parties to notify allegedly illegal conduct or unauthorised sales. Such procedures are in particular put in place in order to allow customer or intellectual property right owners to notify the listing of counterfeit products or otherwise prohibited items on the marketplaces.

(460) The majority of marketplaces (slightly more than 60 %) have specific mechanisms or tools in place providing third parties with the possibility to report such items and request their take down. Some of those that indicate not to have specific notification mechanisms in place are smaller marketplaces that verify the listing of each product manually thereby limiting risks of illegal or counterfeit products being sold on the marketplace. Others contractually oblige retailers not to sell such products and to respect existing rights of third parties.

(461) A number of marketplaces have established specific programs with right owners to establish procedures that facilitate the protection of intellectual property rights, some of which include informing the intellectual property right owners on suspicious listings.

(462) Marketplaces were asked who would generally notify them regarding illegal conduct or unauthorised sale of products. Almost all marketplaces report to receive notifications

from the owners of intellectual property rights (97 %) whereas the majority of marketplaces indicate to receive notifications from competent authorities (73 %), from customers (70 %) and from competitors of the seller (65 %).²⁶⁷ Four out of five marketplaces report to remove items or sellers from the marketplace also on their own initiative, i.e. without a prior complaint from a third party. Items removed are typically prohibited items or items that may infringe third party intellectual property rights.

(463) Sellers are typically removed if they fail to comply with the standards/terms and conditions of the marketplace.

(464) Some retailers stress the importance of the transparency of the process and consider the possibilities of retailers to defend their interest and request review of the decision taken by the marketplace as not sufficient.

4.4.8 Marketplace restrictions under EU competition rules

(465) There is currently a debate, in particular in some Member States, whether marketplace restrictions which are not linked to qualitative criteria (absolute or per se marketplace bans) amount to hardcore restrictions in the form of restrictions of "passive sales" within the meaning of the Vertical Block Exemption Regulation. A reference for a preliminary ruling is currently pending in this regard before the Court of Justice.²⁶⁸

(466) The list of so-called "hardcore" restrictions in Article 4 of the Vertical Block Exemption Regulation describes certain restrictions which do not benefit from the block exemption on the basis of the nature of those restrictions and the fact that they are likely to produce negative effects on the market. The lists of hardcore restrictions contained in Article 4 of the Vertical Block Exemption Regulation reflect the types of agreements, which at the time of its adoption were seen as having as their object a restriction of competition.

(467) The question of whether an absolute marketplace ban constitutes a hardcore restriction within the meaning of Article 4(b) and/or (c) Vertical Block Exemption Regulation has so far not been appraised by the European Courts. As can be seen from paragraph 54 of the Vertical Guidelines, the Commission did – at the time when the Vertical Block Exemption Regulation was adopted – not consider marketplace bans to amount to hardcore restrictions which are incapable of qualifying for a block-exemption.

(468) Based on the Pierre Fabre-judgment of the Court of Justice, a contractual or a de facto ban of the use of the internet as a method of marketing has as its object the restriction of passive sales and can be considered a restriction by object pursuant to Article 101(1) TFEU and a hardcore restriction under Article 4(c) Vertical Block Exemption

²⁶⁷ All proportions are calculated out of the 34 marketplaces that responded to the relevant question.

²⁶⁸ A reference for a preliminary ruling has been put forward by the OLG Frankfurt am Main in Case C-230/16 Coty Germany GmbH vs. Parfümerie Akzente GmbH in which the referring court is essentially asking the Court of Justice whether a ban to use third party platforms which are discernible to the public in a selective distribution agreement may be compatible with Article 101(1) TFEU and whether such a restriction constitutes a hardcore restriction within the meaning of Article 4 (b) and/or Article 4 (c) of the Vertical Block Exemption Regulation.

Regulation.²⁶⁹ If a marketplace ban de facto amounts to a total ban of the use of the internet as a method of marketing, marketplace bans could in line with *Pierre Fabre* be considered as having as its object the restriction of passive sales and as a hardcore restriction under the Vertical Block Exemption Regulation.

(469) The preliminary findings of the sector inquiry do not show that absolute marketplace bans generally amount to a de facto prohibition to sell online irrespective of the markets concerned. Marketplace bans can therefore not be equated to a prohibition to sell via the internet. More specifically, the preliminary findings show that the importance of marketplaces and, consequently, the impact of marketplace bans, vary significantly:

- (a) Own online shops remain the most important online sales channel for retailers. More than half of the respondent retailers sell via their own online shop only. They do not see a need to complement this sales channel by selling also through marketplaces.
- (b) The importance of marketplaces as an online sales channel differs from one Member State to another to a significant extent. While in Germany, more than 60 % of retailers reported to be selling via marketplaces, less than a quarter of retailers did so for other Member States such as Italy, Belgium or Sweden.
- (c) The importance of marketplaces as a sales channel also varies from one product category to another and within product categories. Marketplaces are particularly relevant for retailers selling clothing and shoes and consumer electronics. In contrast, the average proportion of sellers on marketplaces selling household appliances or computer games and software is more limited. The importance of marketplaces as a sales channel also differs depending on the nature of the product and whether customers would expect to find the products for sale on marketplaces.
- (d) Marketplace sales are more important for smaller and medium-sized retailers than for larger retailers. Marketplace bans may therefore affect smaller and medium-sized retailers more. The proportion of retailers selling only via marketplaces is significantly lower for retailers with a turnover above EUR 2 million while smaller and medium sized retailers with a turnover below 2 million are more likely to sell only via marketplaces. The proportion of retailers selling only on marketplaces is highest for retailers with a turnover below EUR 100 000 (11 %). However, even in this turnover category the majority of respondents (54 %) indicated to be selling through their own online shop only. Retailers with a turnover below EUR 2 million that sold on their own online shop as well as on marketplaces also realised

²⁶⁹ Judgment in *Pierre Fabre Dermo-Cosmétique SAS vs. Président de l’Autorité de la concurrence* EU:C:2011:649, paragraphs 47 and 54. See also Vertical Guidelines paragraph 52.

the majority of transactions via marketplaces whereas the majority of transactions of such retailers with a turnover above EUR 2 million were realised on their own online shops.

(470) In addition, according to the manufacturers, the impact of sales via marketplaces on manufacturer's business depends on the type of product as well as particular features of a marketplace.

(471) The preliminary findings of the sector inquiry show that the potential justifications and efficiencies that manufacturers invoke for requesting absolute marketplace bans differ from one product to another:

- (a) Potential efficiencies linked to the protection of a certain brand image may be more relevant for some products and brands than for others.
- (b) For some products, pre-and post-sale service considerations are of greater importance for the products sold and potential free-riding by marketplace sellers may be more prevalent than for products which require only limited pre- and post-sale services.

(472) The preliminary findings of the sector inquiry do not indicate that marketplace bans should be considered hardcore restrictions within the meaning of Article 4(b) and/or Article 4(c) of the Vertical Block Exemption Regulation. The Commission considers that such clauses do not have as their object (i) a restriction of the territory or the customers to whom the retailer in question may sell or (ii) the restriction of active or passive sales to end users. They are not aimed at segmenting markets in the internal market based on territory or customers. Such an approach is in line with the Vertical Guidelines which specify that marketplace restrictions requiring the retailer to use third party platforms (e.g. marketplaces) only in accordance with the quality criteria agreed between the manufacturer and its retailers for the retailer's use of the internet are not considered a hardcore restriction.²⁷⁰ They concern the question of *how* the distributor can sell the products over the internet and do not have the object to restrict *where or to whom* distributors can sell the products.

(473) This does not mean that the Commission considers absolute marketplace bans in all cases compatible with European competition law. The Commission or National Competition Authorities may decide to scrutinize marketplace bans in agreements which fall outside the application of the Vertical Block Exemption Regulation, either because the market share thresholds in Article 3 Vertical Block Exemption Regulation are exceeded or because the agreements contain any of the listed hardcore restrictions in Article 4 of the Vertical Block Exemption Regulation. The Commission or National Competition Authorities may also decide to withdraw the benefit of the Vertical Block Exemption Regulation pursuant to Article 29 of Regulation 1/2003, if in a particular case marketplace bans are restricting competition within the meaning of Article 101(1)

²⁷⁰ See Vertical Guidelines, paragraph 54.

TFEU and are incompatible with Article 101(3) TFEU. The importance of marketplaces as an online sales channel in relation to the product and geographic market in question as well as the credibility of brand protection considerations and the need for pre- and post-sale advice will be important elements in the analysis.

(474) Justifications based on brand protection considerations or on a lack of sufficient pre- or post-sale advice will be less convincing if the manufacturer has accepted the marketplace operator as an authorized seller within its selective distribution agreement or if the manufacturer is itself selling on the marketplace directly to customers.

Summary

The question to which extent restrictions limiting the ability of retailers to sell via online marketplaces may raise concerns under the EU competition rules has attracted significant attention in the past years in some Member States. In this regard, a reference for a preliminary ruling is currently pending before the Court of Justice. One of the aims of the sector inquiry is to better understand the prevalence and characteristics of marketplace restrictions and the importance of marketplaces as a sales channel for retailers and manufacturers.

Marketplace restrictions are not uncommon and 18 % of retailers report to have agreements with their suppliers containing marketplace restrictions. The Member States with the highest proportion of retailers experiencing marketplace restrictions are Germany (32 %) and France (21 %).

Marketplace restrictions encountered in the sector inquiry range from absolute bans to restrictions on marketplaces that do not fulfil certain quality criteria. Restrictions on the usage of marketplaces are mostly found in selective distribution agreements and typically concern branded goods without being limited to luxury or complex or technical goods. They are most widespread in the product categories sports and outdoor (14 % of retailers active in the product category) and clothing and shoes (12 %) followed by consumer electronics (11 %).

Manufacturers provide a number of reasons for restrictions on sales via marketplaces. These relate essentially to the following aspects:

- (a) the protection of the image and the positioning of their brand;
- (b) combatting the sale of counterfeit products on marketplaces;
- (c) ensuring proper pre- and post-sale services by retailers;
- (d) protecting existing distribution channels from free-riding; and
- (e) concerns about the market position of certain marketplaces.

Conversely, many retailers as well as marketplaces allege that manufacturers want to reduce the number of sellers selling online and avoid increased price transparency and increased price competition by introducing marketplace restrictions.

The information obtained in the sector inquiry indicates that the level of importance of marketplaces as a sales channel varies depending on the size of the retailers, the Member States concerned as well as the product categories concerned:

(a) For the majority of retailers (61 %) that responded to the relevant question marketplaces are not important as a sales channel as they sell their products only via their online shop. 31 % of retailers sell via their online shops as well as on marketplaces and only 4 % of the retailers reported to be selling online only via marketplaces.

(b) Marketplaces are more important as a sales channel for smaller and medium-sized retailers with a turnover below EUR 2 million while they are of lesser importance for larger retailers with a higher turnover. The preliminary results show that smaller retailers tend to realise a larger proportion of their sales via marketplaces than larger retailers.

(c) The importance of marketplaces as an online sales channel differs from one Member State to another to a significant extent with a high proportion of retailers using marketplaces in Germany (62 %) and the United Kingdom (43 %) compared to a substantially smaller proportion in Austria (13 %), Italy (13 %) or Belgium (4 %).

(d) The importance of marketplaces differs between the different product categories and within product categories depending on the nature of the product and whether customers would expect to find the products for sale on marketplaces. Marketplaces are most relevant for retailers selling clothing and shoes and consumer electronics.

These preliminary findings do not show that marketplace bans generally amount to a de facto prohibition to sell online irrespective of the markets concerned. The preliminary findings also show that the potential justification and efficiencies that manufacturers invoke differ from one product to another.

In the light of the preliminary findings of these for inquiry, the Commission does not consider (absolute) marketplace bans to constitute hardcore restrictions within the meaning of Article 4(b) and Article 4(c) of the Vertical Block Exemption Regulation as they do not have the object of segmenting markets in the internal market based on territory or customers. They concern the question of *how* the distributor can sell the products over the internet and do not have the object to restrict *where or to whom* distributors can sell the products.

This does not mean that absolute marketplace bans are generally compatible with European competition law. The Commission or National Competition Authorities may decide to scrutinize marketplace bans in agreements falling outside the application of the Vertical Block Exemption Regulation, either because the market share thresholds in Article 3 Vertical Block Exemption Regulation are exceeded or because the agreements contain any of the listed hardcore restrictions in Article 4 Vertical Block Exemption Regulation. The Commission or National Competition Authorities may also decide to withdraw the benefit of the Vertical Block Exemption Regulation if in a particular case the marketplace bans restrict competition within the meaning of Article 101(1) TFEU and are incompatible with Article 101(3) TFEU.

4.5 The use of price comparison tools and restrictions on the use of price comparison tools

- (475) Price comparison tools allow potential customers (in particular those which consider the price as an important buying criterion) to find retailers that offer certain products, compare prices with limited efforts across these retailers and call up the offers they consider suitable. The actual sale does not take place on the website of the price comparison tool, but on the website of the retailer to which potential customers are directed via the website of the price comparison tool, at which point there is no longer any connection to the website of the price comparison tool.
- (476) Price comparison tools allow retailers to increase their visibility, often on a widely used website, and thereby generate traffic on their own website. Compensation paid to price comparison tools by retailers is typically on a pay-per-click basis²⁷¹ and takes place irrespective of whether a sale is ultimately concluded on the website of the retailer or not. The most commonly used means by which price comparison tools obtain relevant pricing and product information is via data feeds from retailers.²⁷²
- (477) On the one hand, price comparison tools increase price transparency and intensify intra-brand and potentially inter-brand price competition between different retailers. On the other hand, some manufacturers are critical of price comparisons tools as they typically focus mainly on price and do not – in the views of these manufacturers - allow retailers to differentiate themselves sufficiently in terms of scope and quality of service which can have a negative impact on the brand image.
- (478) Some agreements between manufacturers and retailers therefore contain contractual restrictions under which the retailers are limited in their ability to actively provide information or otherwise promote their online product offering with price comparison tools.
- (479) The Commission has analysed the usage of price comparison tools by retailers as well as the contractual restrictions encountered in the sector inquiry.

4.5.1 Usage of price comparison tools by retailers

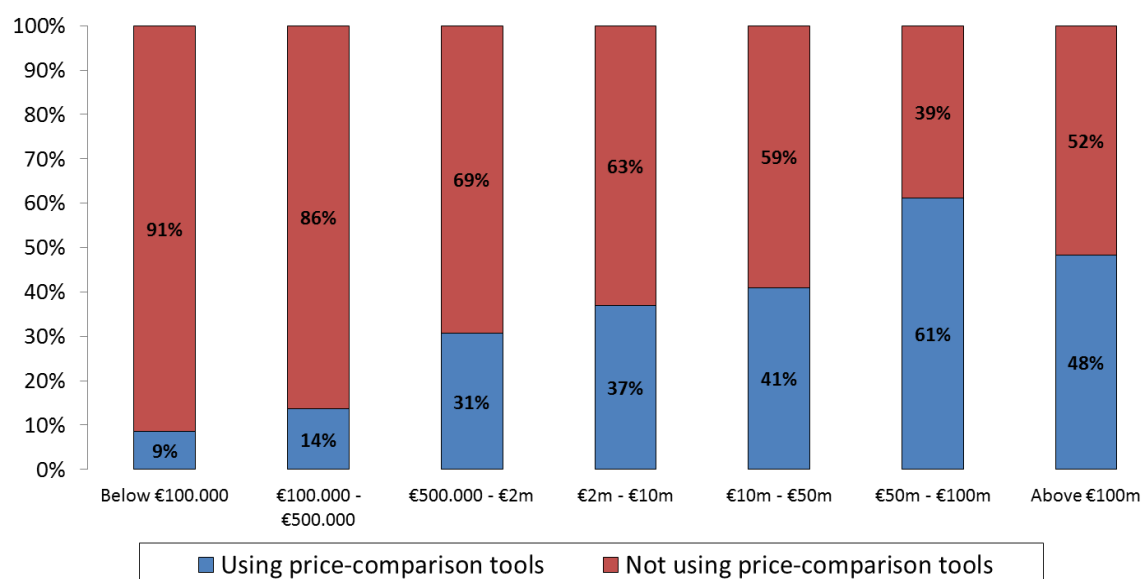
- (480) According to the preliminary findings of the sector inquiry, the use of price comparison tools is widespread. 36 % of retailers reported that they supplied data feeds regarding their products to price comparison tool providers in 2014.²⁷³ As shown in Figure B. 68 below, larger retailers (in terms of turnover) are more likely to use price comparison tools than smaller ones.

²⁷¹ See section B.1.4 Price comparison tools on characteristics of respondent price comparison tools.

²⁷² See section B.1.4 Price comparison tools on characteristics of respondent price comparison tools.

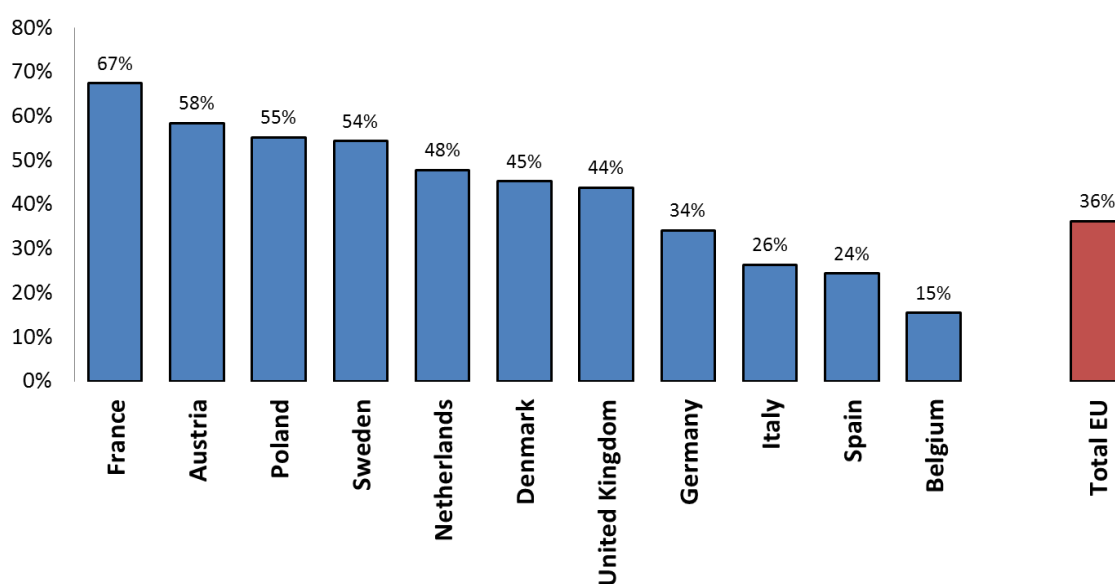
²⁷³ Figures are calculated based on all respondents to the relevant question, namely 1013.

Figure B. 68: Proportion of retailers in each turnover category that use price comparison tools²⁷⁴



(481) The proportion of retailers that use price comparison tools differs considerably across different Member States (see Figure B. 69) and in some Member States more than half of the retailers reported using price comparison tools.

Figure B. 69: Proportion of retailers in each EU Member State using price comparison tools²⁷⁵



(482) The average number of retailers listing their product offering on the price comparison tools that provided information to the relevant question in 2014 was almost 4 000.²⁷⁶

²⁷⁴ Proportions are calculated out of all respondents in a given turnover category (on the basis of 2014 turnover) who responded to the relevant questions. In total 994 retailers provided the respective information.

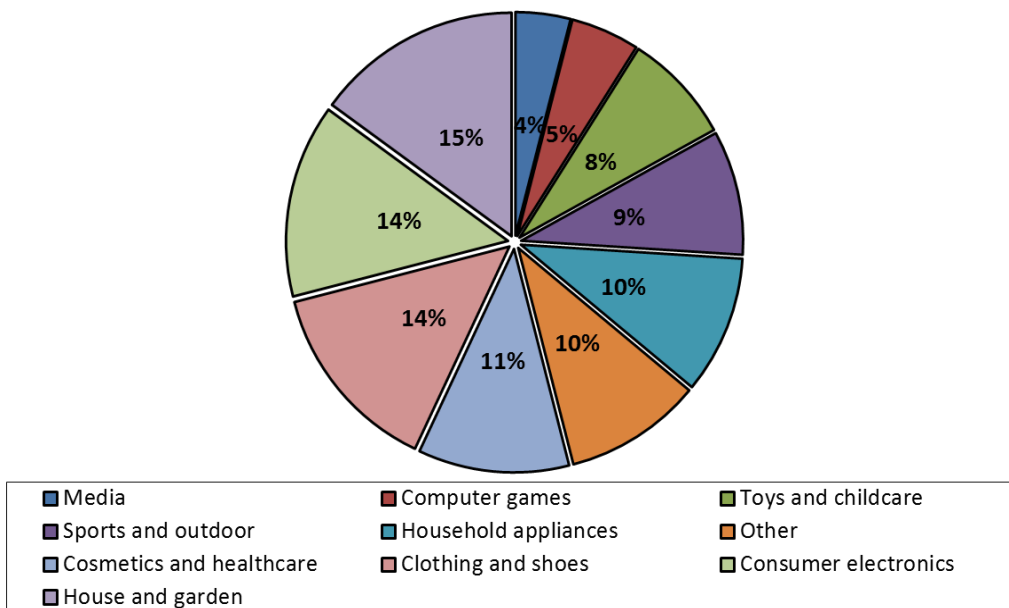
²⁷⁵ The proportion at the EU level is calculated out of all retailers who replied to the relevant question, namely 1013. Proportions at the Member State level are calculated out of all retailers that responded to the relevant question from the respective Member State. Only Member States with a minimum of 20 respondent retailers were taken into account.

Between 2012 and 2014, the number of registered retailers and/or retailers whose product offerings were listed on the price comparison tools has on average increased by almost 240 %.

(483) The average conversion rate reported by the retailers realized via links from price comparison tools is 3 %²⁷⁷, which is lower than the average conversion rate on retailers' own website (4 %) and marketplaces (5 %).

(484) Generally, price comparison tools are not specialised in a certain product category. In fact, the preliminary findings show that an average price comparison tool offers a comparison of products in eight of the relevant product categories.²⁷⁸ However, as shown in Figure B. 70, there are some differences in the number of registered retailers across the different product categories. Moreover, in terms of number of clicks on the product listings on price comparison tools one can observe similar differences among product categories (see Figure B. 71). More precisely, the figures show that for clothing and shoes, consumer electronics and house and garden products the use of price comparison tools is more prominent than for the product categories media and computer games and software.

Figure B. 70: Average proportion of sellers on price comparison tools in each product category²⁷⁹



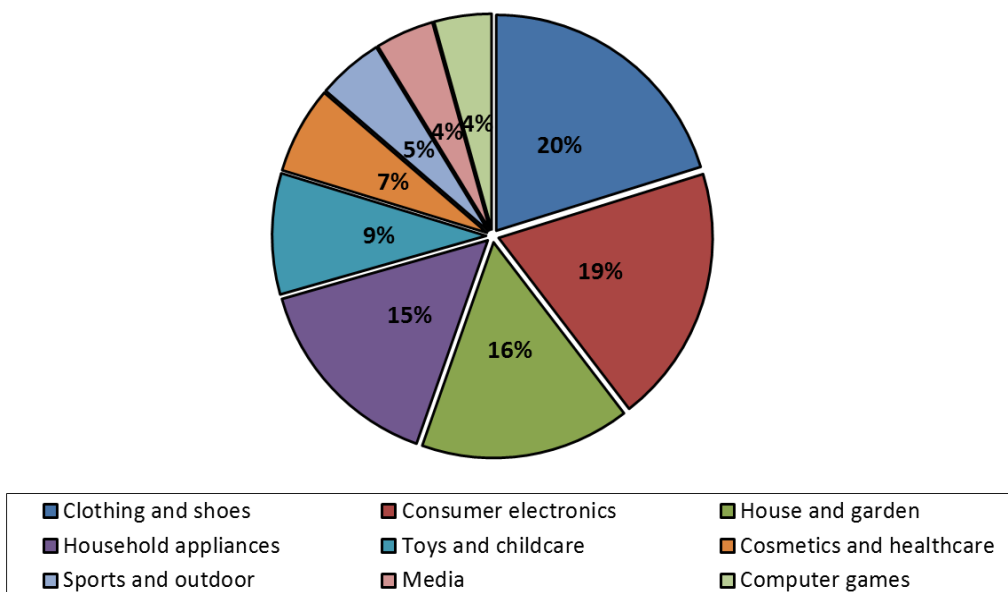
²⁷⁶ Figures are calculated based on the responses of 48 price comparison tools.

²⁷⁷ Figures are calculated based on all retailers who provided data regarding the relevant question, namely 260.

²⁷⁸ Figures are calculated based on the responses on 88 price comparison tools.

²⁷⁹ Proportions are calculated based on the responses of 36 price comparison tools. The proportions per product category are calculated as the (simple) average of the proportion of sellers in the respective product category across respondents.

Figure B. 71: Average proportions of visits on price comparison tools in each product category²⁸⁰



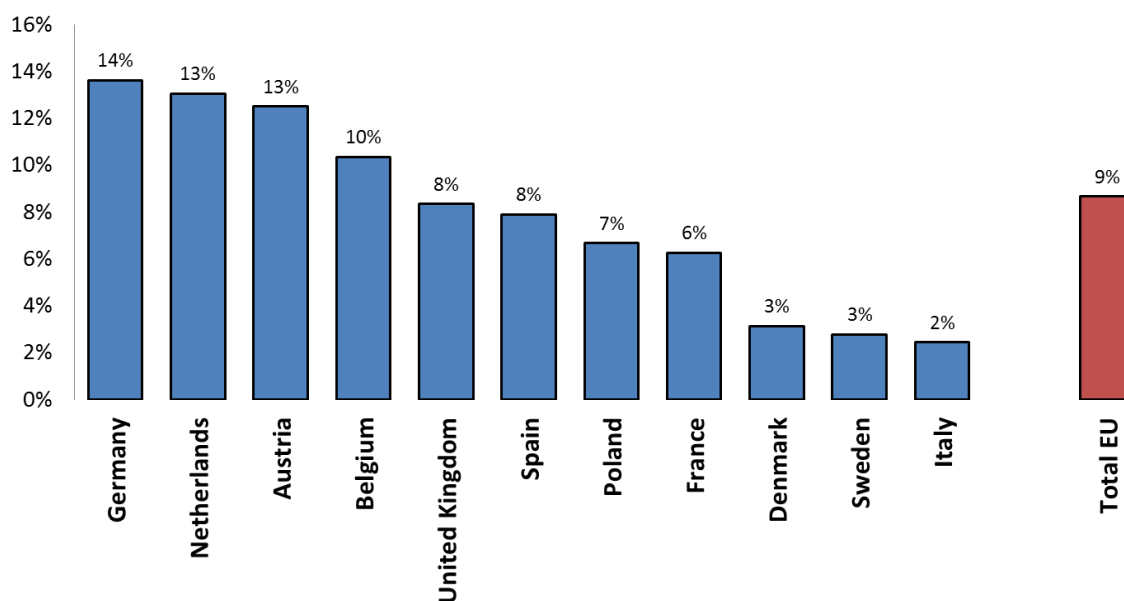
4.5.2 Restrictions on the use of price comparison tools

(485) Some agreements between manufacturers and retailers include contractual restrictions with regard to the use of price comparison tools. 9 % of respondent retailers reported that they have agreements with manufacturers which contain some form of restriction in their ability to use price comparison tools.

(486) As can be seen from Figure B. 72, the proportion of retailers that have agreements containing some form of price comparison use restrictions differs between Member States. Retailers which are active in Germany and the Netherlands are most affected by the restrictions to use price comparison tools. Restrictions on the use of price comparison tools are not related to the observed frequency of the use of price comparison tools by retailers in a Member State (see Figure B. 69 above).

²⁸⁰ Proportions are calculated on the basis of the replies of 30 price comparison tools who supplied information on 2412 top retailers. The proportions per product category are calculated as the (simple) average across respondents of the proportion of visits in the respective product category out of the total visits reported by a respondent.

Figure B. 72: Proportion of retailers in each EU Member State that have agreements containing a restriction to use price comparison tools²⁸¹



(487) Retailers were questioned about the type of restrictions they have. Based on these responses, the most widespread type of restriction to use price comparison tools is a prohibition to use any price comparison tool, which is encountered by 5 % of the retailers.²⁸² Other types of restrictions, such as restrictions based on certain quality criteria of a price comparison tool are used to a lesser extent.

(488) The review of the agreements provided in the context of the sector inquiry shows that there are different contractual clauses which may limit the ability of retailers to use price comparison tools to promote their product offering and attract (potential) customers to their website. They include among others the following types of provisions:

- (a) restrictions to use, sell or promote on any price comparison tool;
- (b) restrictions to actively provide price and product information to price comparison tools;
- (c) restrictions to use price comparison tools targeting customers in other (in some cases exclusively allocated) territories;
- (d) restrictions to use price comparison tools that present individual products and prices (which is typical for price comparison tools) rather than a whole range of products offered by the manufacturer; and

²⁸¹ Proportions are calculated out of all retailers that responded to the questionnaire from the respective Member State. Only Member States with a minimum of 20 respondent retailers were taken into account.

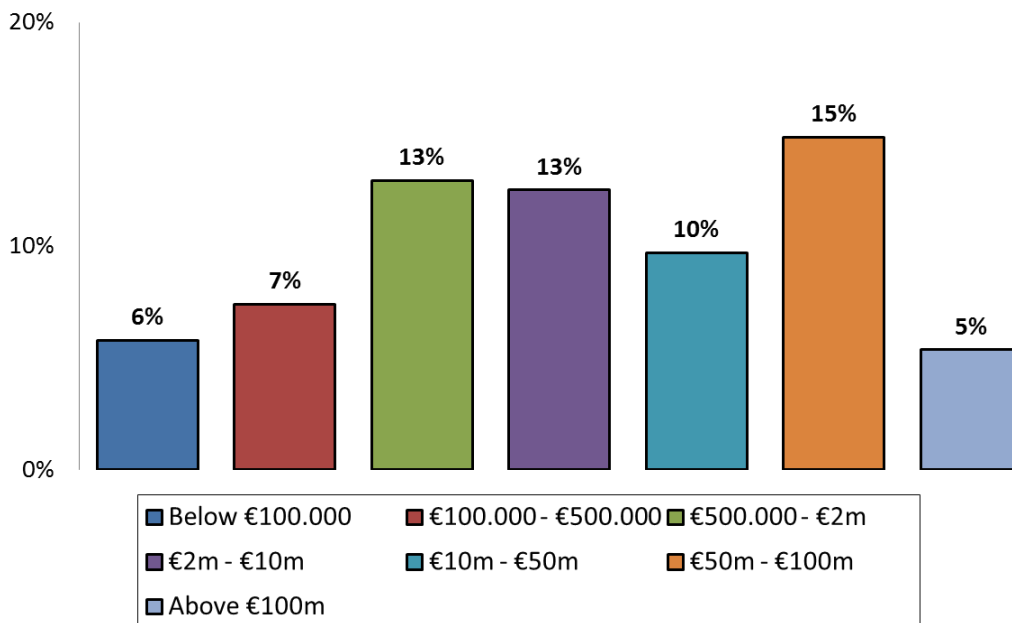
²⁸² Proportions are calculated out of all 1051 retailers that responded to the questionnaire.

- (e) restrictions on the use of the brand name or of any information/pictures provided by the manufacturer in connection with price comparison tools or for marketing purposes in general.

(489) In some instances, the restrictions are not formulated as outright prohibitions, but as requirements, whereby approval by the manufacturer is needed, before the use of price comparison tools is allowed. The Commission preliminarily considers that the result of such an approval requirement may be the same as an outright prohibition as retailers may either not request approval or their request may be denied. In some cases, retailers need to confirm in writing that they will not use price comparison tools in order to be admitted as a member of the selective distribution network of the manufacturer.

(490) As shown in Figure B. 73, the initial findings in the sector inquiry do not indicate any relation between the size of the retailer and the likelihood of having a restriction to use price comparison tools.

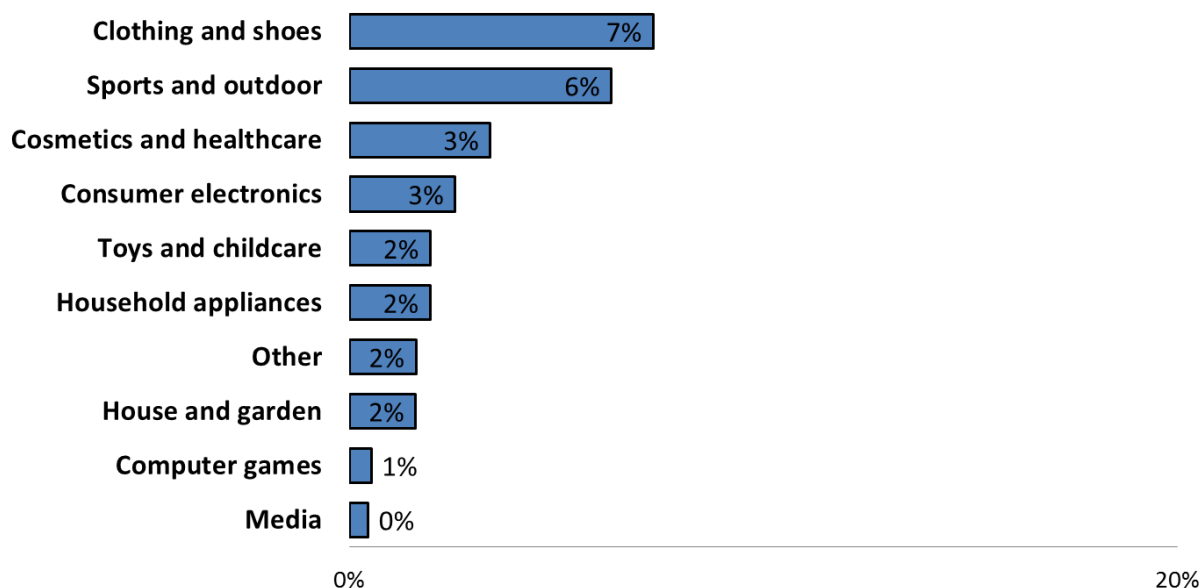
Figure B. 73: Proportion of retailers in each turnover category that have agreements containing restrictions to use price comparison tools²⁸³



(491) There are, however, some differences when it comes to the prevalence of restrictions to use price comparison tools across different product categories. Product categories, for which the use of price comparison tools is least widespread, such as media and computer games and software, are also product categories in which there are the least restrictions.

²⁸³ Proportion are calculated out of all retailers that responded to the relevant question in each of the turnover categories. This number ranges from 74 retailers for the turnover category EUR 50 million to EUR 100 million to 299 retailers for the turnover category above EUR 100 million.

Figure B. 74: Proportion of retailers in each product category that have agreements containing restrictions to use price comparison tools²⁸⁴



(492) Less than 20 % of price comparison tools have reported that they are aware of restrictions on retailers' ability to list product offerings on their price comparison tool which are contained in the agreements with the manufacturers of the products in question.²⁸⁵

4.5.3 Reasons put forward for restrictions to use price comparison tools

(493) When asked about the potential impact of price comparison tools on their business, 32 % of manufacturers that responded to the questionnaire indicated that they consider them as having a potentially adverse impact on their business whereas 29 % stated that they consider them as having a potentially beneficial impact on their business. There is quite some divergence between the various product categories. For example, in consumer electronics the majority of manufacturers consider them as having a potentially beneficial impact (60 %) and only a much smaller proportion (21 %) considers them as potentially having an adverse impact on their business.²⁸⁶ Conversely, in clothing and shoes, 43 % of manufacturers consider them as potentially having an adverse impact for their business whereas only 17 % consider them as potentially having a beneficial impact.

(494) Manufacturers that consider price comparison tools as good for their business point out that customers increasingly use them to take or prepare purchasing decisions. Price comparison tools allow potential customers to find (authorized) retailers and direct them to their websites. They enhance visibility for the brand on the internet and often provide

²⁸⁴ Proportions are calculated out of all retailers that indicated sales in the respective product category.

²⁸⁵ Figures are calculated based on all 86 respondents to the question.

²⁸⁶ Proportions are calculated out of all respondents which are active in the respective product category. See also Figure B. 21 and Figure B. 22.

product and seller reviews which further inform customers about the products and the sellers.

- (495) A substantial number of manufacturers see price comparison tools rather critically. According to these manufacturers price comparison tools focus only on price which is not necessarily the most important element for the attractiveness of their product and other factors are equally affecting the choice of the customer (luxurious image, quality, features, and style). In addition, it is difficult for retailers to differentiate themselves in terms of service quality and delivery/return options on price comparison tools and retailers with low service quality might free-ride on other retailer's investments. Low service quality could negatively reflect on the brand image. On some price comparison tools authentic products and their prices may also be compared with second hand or counterfeit products which again could damage the brand image.
- (496) Some manufacturers point out that price comparison tools intensify competition on price – not on other parameters – and may contribute to making customers increasingly price sensitive. They may create downward pressure on prices and reduce margins if retailers are starting to undercut each other's prices to feature prominently on price comparison tools. This may be detrimental for specialised retailers with brick and mortar shops (but also specialised online retailers) which have higher cost structures because of the additional services they provide. While price comparison tools may therefore increase sales in the short term, they may reduce incentives of specialised retailers to invest in quality and services and lead to a reduced number of retailers in the long run.
- (497) According to price comparison tools, the most quoted reasons for limiting the use of price comparison tools by the manufacturers are protection of the brand image and the quality standard of distribution. Most price comparison tools do not consider these reasons to be justified. They claim that price comparison tools provide objective information on features and reviews of products which do not interfere with brand image or the quality of product distribution. Most price comparison tools offer the possibility to the retailers to display their logo as well as product pictures on their website. Some of them offer customer reviews and additional product-related information as well as information on delivery times.
- (498) Moreover, more than 90 % of the price comparison tools have taken particular steps in the last few years to increase the quality and the image of the services, which they offer. Some examples include improved layout of the website, increase in the number of retailers, use of videos, inclusion of expert reviews, improved accuracy of information provided on the website, improved functionality of the website, optimisation of search relevance, ability for retailers to include promotions of certain products, support of better quality product images, marketing campaigns, compatibility with mobile phones and tablets, increased frequency of information update, improved interface with the retailers, fraud monitoring and protection programmes for customers.

(499) Many retailers confirm that protecting the brand images as well as the quality of service are among the reasons most frequently put forward by manufacturers with regard to the contractual restriction limiting the retailer's ability to use price comparison tools. Some retailers consider that the main aim of manufacturers is to decrease price transparency and limit price competition among retailers, in some case also in order to protect their own online offering.

4.5.4 Restrictions on the use of price comparison tools under EU competition rules

(500) Marketplaces and price comparison tools differ in a number of respects, including the fact that no transaction takes place on the price comparison tool's website/app. Instead interested potential customers are being directed to the website of the (authorised) distributor from which the product can be purchased and which generally fulfils all the quality criteria requested by the manufacturer of the product (within its selective distribution system).

(501) Price comparison tools are therefore not a distinct online sales channel, but offer retailers the ability to present their online offerings on a widely used website and thereby increase the findability of their online offering and generate traffic on their own website. Customers can filter out those offers they consider suitable based on the information provided on the price comparison tool.²⁸⁷ They can then access the websites of these retailers and compare their offerings, if desired.

(502) Absolute or per se price comparison tool bans which are not linked to quality criteria, limit the ability of distributors to use this promotion method in order to generate traffic for their own website. Such bans may make it more difficult for (potential) customers to find the retailers website and may thereby limit the (authorized) distributor's freedom to promote its online offer. Such bans may make it more difficult to attract (potential) customers outside the physical trading area of the retailer via online promotion. While such general bans may be a cost effective way to prohibit the use of a promotion channel deemed not fitting for the product in question, they may also exclude an effective method for retailers to generate traffic to their website, which is providing (potential) customers increased price transparency across a range of different retailers.

(503) Restrictions on the usage of price comparison tools based on objective qualitative criteria may be used more often to generate efficiencies. Manufacturers operating selective distribution systems are in principle allowed to require quality standards in relation to the promotion of their products on the internet.

(504) Price comparison tools can also allow retailers to specifically target (potential) customers in certain territories outside their home Member State. In these cases, price comparison tools may be used to actively sell into certain other Member States.

²⁸⁷ While the price may be an important element for the customer in its choice, other features of price comparison tools such as customer reviews concerning products or sellers may also be of relevance.

Summary

Price comparison tools allow (potential) customers to find retailers that offer certain products, compare prices with limited efforts across these retailers and call up the offers they consider suitable. The actual sale does not take place on the website of the price comparison tool, but on the website of the retailer to which customers are directed via the website of the price comparison tool.

The Commission has analysed the usage of price comparisons tools by retailers and the contractual restrictions limiting their ability to use such tools.

The preliminary findings of the sector inquiry indicate that the use of price comparison tools is widespread with 36 % of retailers reporting that they supplied data feeds to price comparison tool providers in 2014.

Larger retailers (in terms of turnover) are more likely to use price comparison tools than smaller ones. The use of price comparison tools is more prominent for some product categories than for other, with the product categories clothing and shoes, consumer electronics and house and garden being the product categories in which price comparison tools are most relevant.

9 % of retailers reported that they have agreements with manufacturers which contain some form of restriction in their ability to use price comparison tools.

Restrictions on the usage of price comparison tools encountered in the sector inquiry range from absolute bans to restrictions based on certain quality criteria.

A substantial number of manufacturers see price comparison tools rather critically as they focus only on price which is not necessarily the most important element for the attractiveness of their product and other factors are equally affecting the choice of the customer (luxurious image, quality, features, and style).

Marketplaces and price comparison tools also differ in a number of respects, including the fact that no transaction takes place on the price comparison tool's website/app. Instead interested customers are being directed to the website of the (authorised) distributor from which the product can be purchased and which generally fulfils all the quality criteria requested by the manufacturer of the product (within its selective distribution system).

Absolute or per se price comparison tool bans which are not linked to quality criteria, may limit the ability of distributors to use this promotion method in order to generate traffic for their own website. Bans to use price comparison tools may make it more difficult for customers to find the retailer's website thereby potentially limiting the (authorized) retailer's freedom to promote its own online offer. Such bans may make it also more difficult to attract customers outside the physical trading area of the retailer via online promotion. While such general bans may be a cost effective way to prohibit the use of a promotion channel deemed not fitting for the product in question, they may also exclude an effective method for retailers

to generate traffic on their website that is providing (potential) customers increased price transparency across a range of different retailers.

Restrictions on the usage of price comparison tools based on objective qualitative criteria may be used more often to generate efficiencies. Manufacturers operating selective distribution systems are in principle allowed to require quality standards in relation to promoting their products on the internet.

4.6 Pricing restrictions

(505) The Commission has asked retailers to provide information in relation to their pricing policies and the role of manufacturers in their price setting. Manufacturers, in turn, were asked about their input to retailers' pricing policies.

4.6.1 Price setting at retail level

(506) The practice of recommending a resale price or requiring the retailer to respect a maximum resale price is covered by the Vertical Block Exemption Regulation provided that the market share thresholds set out in the regulation are not exceeded.²⁸⁸

(507) However, it is important that manufacturers do not take action that interferes with the freedom of retailers to set their final prices to customers by making the recommended retail price or the maximum retail price equivalent to a minimum or fixed price. As provided for in the case-law²⁸⁹ and in the Vertical Block Exemption Regulation, agreements that establish a minimum or fixed price (or price range) are a restriction of competition by object under Article 101(1) TFEU and a hardcore restriction within the meaning of Article 4(a) of the Vertical Block Exemption Regulation.

(508) In case of price recommendations, concerns could arise if such recommended retail prices translated into an agreement or concerted practice between the manufacturer and the retailer, leading the retailer to stick to the recommended retail prices when setting its actual price to customers. Such agreements, whether achieved via direct (explicit contractual) or indirect means (typically, as a result of pressure by manufacturers), amount to a hardcore restriction under Article 4(a) of the Vertical Block Exemption Regulation.²⁹⁰

(509) Retailers were asked whether manufacturers provide certain pricing recommendations or specify other parameters affecting the prices set by retailers to customers. 38 % of retailers report that manufacturers recommend resale prices, while less than 10 % report being provided with a discount range or receiving indications from manufacturers to

²⁸⁸ See Vertical Guidelines, paragraph 226.

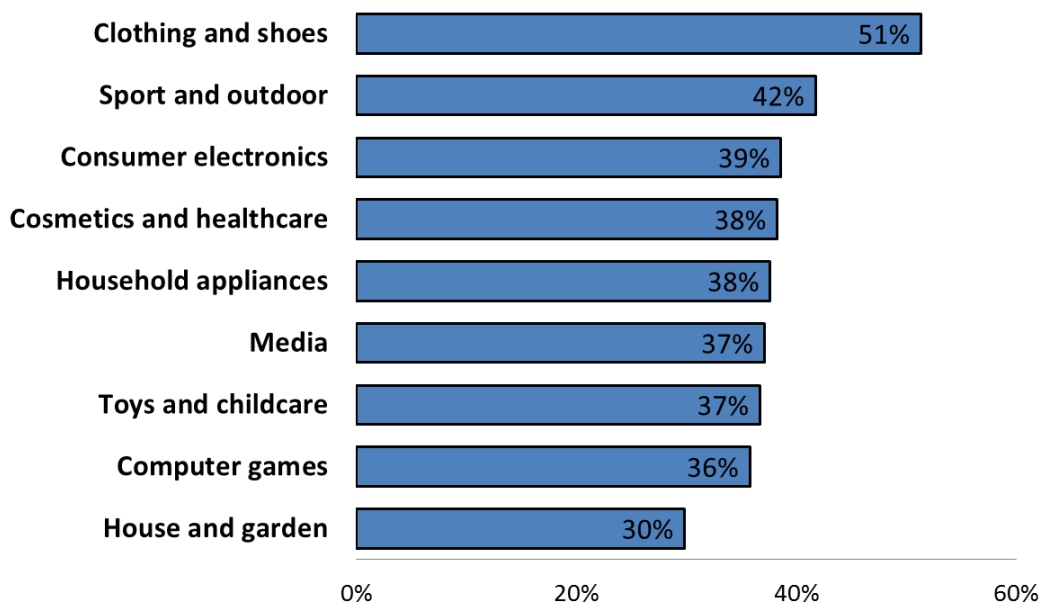
²⁸⁹ See judgment in *SA Binon Cie v SA Agence et Messageries de la Presse*, 243/83, EU:C:1985:284, paragraph 43; judgment in *ASBL Vereniging van Vlaamse Reisbureaus v ASBL Sociale Dienst van de Plaatselijke en Gewestelijke Overheidsdiensten*, 311/85, EU:C:1987:418, paragraph 17; judgment in *SPRL Louis Erauw-Jacquery v La Hesbignonne SC*, 27/87, EU:C:1988:183, paragraph 15.

²⁹⁰ On resale price restrictions, see paragraphs 223 to 229 of the Vertical Guidelines.

apply the same retail price online and offline.²⁹¹ A smaller proportion of retailers receive indications of what minimum price they should apply or which advertised price they should use.²⁹²

(510) Looking at the responses per product category (see also Figure B. 75 below), at least a third of the retailers in each product category (with the exception of house and garden) receive some form of price recommendations from manufacturers. The highest proportion of retailers that do so are those active in clothing and shoes, followed by those selling sports equipment and then consumer electronics.

Figure B. 75: Proportion of retailers that reported pricing recommendations per product category²⁹³



(511) Manufacturers report about an even more widespread use of recommended retail prices: four out of five manufacturers use price recommendations to distributors.²⁹⁴

(512) To better understand why pricing recommendations are so widespread, manufacturers were asked to explain the main considerations behind the decision to recommend retail prices to distributors.

(513) Manufacturers express the view that the price of a product is the most immediate way to communicate its quality to the customers and have provided a number of reasons for recommending retail prices.

²⁹¹ 8 % of retailers reported to be provided with a discount range while 7 % retailers reported receiving the indication from manufacturers to apply the same retail price online and offline. Proportions are calculated out of all 1051 responses to the questionnaire.

²⁹² 5 % of retailers reported receiving indications of what minimum price they should apply while 3 % stated they received indications about what advertised price they should use.

²⁹³ Proportions are calculated out of all retailers active in a given product category.

²⁹⁴ Proportions are calculated out of all manufacturers (251) that responded to the questionnaire.

- (514) First of all, manufacturers explain that an important factor taken into consideration when setting the recommended retail price of a product is the intended positioning of the brand or of the specific product. This is reported to be particularly important for premium products and for luxury brands, although manufacturers active in all product categories have argued that there is a strong link between recommended retail prices and brand/product positioning. The level of recommended retail prices is chosen in order to reflect a certain brand/product image or to strengthen the image or its perceived value.
- (515) Manufacturers further explain that products tend to be designed and manufactured taking already into consideration an estimated retail price level. Therefore, their investments in research and development as well as other manufacturing costs are inextricably linked to a given recommended retail price.
- (516) Recommended retail prices are set also on the basis of market studies that allow manufacturers to gauge customers' willingness to pay. Manufacturers state that they have a better understanding than retailers of the price a customer would be prepared to pay for their products and, therefore, are better placed to evaluate market conditions and develop a marketing strategy, which includes the price of the products. Market knowledge is particularly important when a product is launched as manufacturers explain.
- (517) Another reason brought forward is that manufacturers either believe that retailers need price guidance or that they receive requests from retailers for such guidance. Many manufacturers have explained that they provide recommended retail prices in order to help retailers to position manufacturers' products next to many other competing products. According to manufacturers, recommended retail prices can also help independent retailers to compare their prices against the manufacturers own retail activities.
- (518) Along the same lines, manufacturers explain that recommended retail prices may help avoiding or reducing cannibalization across channels and geographies. Some manufacturers consider it important to support the brick-and-mortar channel by preventing online prices from falling below a certain level. Recommended retail prices can help in this regard. Furthermore, when setting the recommended retail prices, manufacturers indicate that they also build-in an estimated profit margin for the retailer.
- (519) Manufacturers also elaborate on what types of products warrant for recommended retail prices. Although few argue that recommended retail prices may be necessary in relation to all types of products, more often the use of recommended retail prices is linked to the launch of new products or to the sales of premium brands/products. For this type of products, it is argued that the price should reflect the quality of the product. When a service is directly related to the sale of the product, manufacturers explain that the recommended retail prices would take this into account as well.

- (520) Beyond price recommendations, retail prices are set by the retailers with a view to achieving a certain expected profit margin.
- (521) In this regard, several manufacturers emphasised the strong negotiating position of large retailers / groups of retailers. Several retailers²⁹⁵ explicitly report about contractually guaranteed profit margins which shift, at least to a certain extent (depending on the individual agreements), the commercial risk back to the supplier.
- (522) Due to their strong negotiating power, certain retailers can, as explained by a number of manufacturers, also obtain ad hoc negotiated compensations for lower profit margins as compared to the expected level of profit margins, leading to a de facto guarantee of profit margins.
- (523) Guaranteed profit margins and occasional compensations of losses or of decreased profit margins may put increasing pressure on manufacturers to ensure a minimum retail price level throughout their distribution network and thereby minimise the risk of compensations to retailers.

4.6.2 Monitoring of recommended retail prices

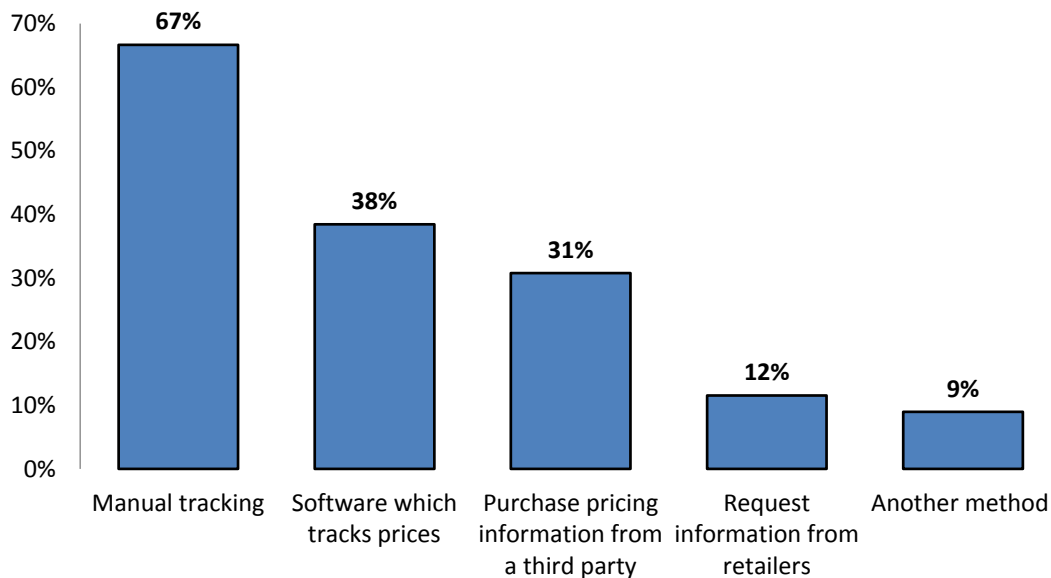
- (524) One aspect relevant for the assessment of recommended retail prices under Article 101 TFEU is whether manufacturers that use recommended retail prices monitor retail prices in order to ensure compliance with pricing recommendations. Such monitoring of retail prices by manufacturers may be a first step leading to subsequent attempts to influence price setting at retail level.
- (525) The Commission therefore asked, on the one hand, retailers - whether they were aware that manufacturers would monitor their compliance with recommended retail prices and what would be the most common way to do so - and, on the other hand, manufacturers - whether they monitor retail prices and, if they do, via what means and for what reason.
- (526) Approximately 18 % of retailers report that manufacturers monitor their retail prices. According to retailers, the most common ways used by manufacturers are visiting the retailers' brick and mortar store or website, obtaining information via an external company, such as a market analyst or companies specialised in tracking prices, or by using dedicated software that would crawl the internet to gather price data, or simply based on complaints from other retailers.
- (527) Nearly 30 % of manufacturers indicated that they systematically track the online retail prices of their products sold via independent distributors.²⁹⁶ Others reported that they would not do so systematically but in a targeted manner. Targeted monitoring, manufacturers explain, tends to focus on premium products and key markets.

²⁹⁵ 14 retailers reported about contractually guaranteed profit margins. Many of them are active in at least two product categories, and indicated guaranteed profit margins in several product categories, with different manufacturers.

²⁹⁶ Based on the responses of 245 manufacturers who replied to this question.

(528) Manufacturers, which indicate that they monitor the retail prices of independent distributors, also provide information on the methods they use for that purpose. The most commonly used method is manual tracking, with two thirds of the manufacturers (out of those that monitor retail prices) making use of such method, followed by the use of price-tracking software.

Figure B. 76: Most commonly reported methods to monitor retail prices by manufacturers²⁹⁷



(529) Manufacturers provided a wide range of reasons to explain why they monitor retail prices.

(530) One of the main reasons given is that monitoring retail prices allows manufacturers to better understand market trends and how successful a given product may be. Some manufacturers explain that they look at their products and competitors' products in order to determine future recommended retail prices, brand/product positioning, as well as calculating manufacturing costs of future products. Monitoring also provides indications to manufacturers as to the price expectations customers have for particular products and to the price pressure by competitors.

(531) In addition, manufacturers that are, vis-à-vis certain retailers, under a contractual or de facto constraint to guarantee a minimum profit margin or to compensate for certain losses or lower profit margins, also have a direct interest in monitoring retail price levels.

(532) Another reason to monitor retail prices is the medium- or long-term impact of the retail price level of a product on the wholesale prices. In general, the level of retail prices affects wholesale prices that are set with a view to the expected achievable retail prices

²⁹⁷ Based on the responses of 78 manufacturers who replied to this question. Each respondent could provide multiple responses, should they use multiple methods to track prices.

(often by using a multiplier) and therefore the expected profit margin. 3 % of the manufacturers report that their wholesale prices are contractually linked to the resale price of their products.²⁹⁸

4.6.3 Retailers' compliance with price indications and reasons

(533) Retailers were asked whether they typically comply with manufacturers' pricing indications. Out of those retailers that replied to the relevant question,²⁹⁹ almost a third reports they normally comply with price indications given by the manufacturers while slightly more than a quarter would not comply. The remaining retailers report compliance with manufacturers' pricing indications would depend on the specific circumstances.³⁰⁰

(534) The responses of the retailers indicate three main reasons for complying with manufacturers' pricing indications:

(535) First, retailers follow pricing indications because they find it profitable. Certain retailers explain, for instance, that, on certain occasions, manufacturers' price indications allow them to obtain a good margin and the price indicated would be in line with market expectations.

(536) Second, retailers, especially smaller ones, decide to comply with the pricing indications because they do not want to damage their business relationship with the manufacturers. For instance, some retailers report that when pricing indications are not followed, manufacturers would contact them and put pressure on them to align their prices. Subsequently, these retailers would tend to accept and follow the indications they receive.

(537) Finally, some retailers follow manufacturers' pricing indications because of explicit threats or retaliatory measures taken by manufacturers in case the retailer would not comply with those indications. Retailers active in the product categories of clothing and shoes, consumer electronics, as well as house and garden, reported more commonly actions by manufacturers to ensure compliance with pricing indications. The main measures retailers referred to were loss of discounts, delayed supplies, severance of contracts or expulsion from the distribution network.

(538) Retailers report that interference with retail prices would typically occur via emails or other means of online communication or, more frequently, via direct phone calls by the manufacturer to the employees of the retailers responsible for pricing.

(539) Several manufacturers emphasise that certain retailers would monitor competing retailers' resale prices and pressure the manufacturers to intervene vis-à-vis low pricing competitors, with a view to achieving the expected profit margins.

²⁹⁸ Proportions are calculated out of all 242 manufacturers that responded to the relevant question.

²⁹⁹ Proportions are calculated out of the responses by 410 retailers that responded to the relevant question.

³⁰⁰ Proportions are calculated out of all retailers (411) that responded to the relevant question.

(540) Certain pricing arrangements between manufacturers and their retailers may merit further investigation on a case-by-case basis.

4.6.4 Charging different wholesale prices for different sales channels

(541) Another way manufacturers can influence retail prices is by charging different wholesale prices to retailers depending on the channel where the product is intended to be resold. Different prices between the different sales channels may take various forms such as a discount mechanism whereby a manufacturer would grant a discounted price for products sold in one channel while no discount would be granted for the same product in the other sales channel.

(542) As already mentioned under section B.2.3 above, 2.5 % of retailers reported that they pay a different price depending on whether the product would be sold online or offline. Only half of those reported that they were passing these differences on to customers in the retail price.

(543) Agreements whereby a distributor has to pay a higher price for products intended to be sold online than for products intended to be sold offline ("dual pricing"), may lead to limiting the retailer's online sales and hinder access to more and different customers online. Such agreements are in principle considered to be hardcore passive sales restrictions.³⁰¹

(544) However, such agreements may, depending on the circumstances, fulfil the conditions of Article 101(3) TFEU and benefit from an individual exemption from the application of Article 101(1) TFEU. One of the key considerations in relation to different discounts offered to different channels is whether the discount is offered to compensate higher costs incurred by the manufacturer as a result of retail sales in one channel and not in the other.³⁰² The granting of a fixed fee compensating for higher costs of one channel as compared to the other is one possibility to compensate for such costs, contrary to variable fees which are considered as liable to incentivise sales via one channel.³⁰³

(545) In this regard, several actors at both the manufacturing and retail level indicate that manufacturers are often trying to find a way to create a level-playing field for the different online/offline sales channels taking into consideration the differences in cost levels of those channels.

(546) Setting different wholesale prices is, however, rarely considered as a viable option due to the risk that such a dual pricing strategy could be in breach of Article 101(1) TFEU.

(547) Some manufacturers emphasised the significant practical difficulties in linking a given wholesale price to the actual costs borne by the retailer, as opposed to offering a general discount, as percentage of the overall sales value, for one of the sales channels. For

³⁰¹ See paragraphs 52 and 64 of the Vertical Guidelines.

³⁰² See paragraphs 52 and 64 of the Vertical Guidelines.

³⁰³ See paragraphs 52 and 64 of the Vertical Guidelines.

instance, in order to know the actual cost of the services provided by the staff for the sale of a certain brand, in a multi-brand brick and mortar shop, the retailer would have to relate and compute the services provided for each sale to each brand (where one single buyer can also buy several brands), making the functioning of the sales points highly inefficient.

(548) In addition, when differentiating between online and offline wholesale prices, manufacturers also show a preference for systems which incentivise retailers to sell more and do not grant them an "ex ante", fixed benefit (with an up-front reduced wholesale price). Manufacturers would rather link such benefit to the actual level of services or other investments that will have played a role in the level and quality of the generated sales.

4.6.5 Online price transparency and the use of price monitoring software

(549) As pointed out in section B.2.3, online price transparency, as one of the main features of e-commerce, has a significant impact on the behaviour at all levels of the supply chain.

(550) About half of the retailers track online prices of competitors.³⁰⁴ In addition to easily accessible online searches and price comparison tools, both retailers and manufacturers report about the use of specific price monitoring software, often referred to as "spiders", created either by third party software specialists or by the companies themselves. This software crawls the internet and gathers large amounts of price related information. 67 % of those retailers that track online prices³⁰⁵ use (also) automatic software programmes for that purpose. Larger companies have a tendency to track online prices of competing retailers more than smaller ones.

(551) Price monitoring software can provide a high level of granularity, scope and immediate access to pricing data. For instance, some software allows companies to monitor several hundred online shops extremely rapidly, if not in real time. Reports can be brand-specific, product-specific or both. Reports can also provide an overview of how much prices diverge from the recommended retail prices, or another reference price used, and for how long. Alert functionalities in price monitoring software allow companies to get alerted as soon as a retailer's price is not in line with a predefined price.

(552) The majority of those retailers that use software to monitor prices, adjust consequently their own prices to those of their competitors (78 %).³⁰⁶ Most of them adjust prices manually (43 %), but some (8 %) use automatic price adjustments based on pricing software programmes (often the same software as the "spider" price monitoring software) and a significant number (27 %) uses both manual and automatic price adjustments. Automatic price adjustments allow the retailer to automatically set certain

³⁰⁴ Based on the 1051 retailers who responded to the questionnaire.

³⁰⁵ 515 retailers have reported to track online prices of competitors.

³⁰⁶ Based on the responses of 343 retailers who responded they were using software to track prices.

product prices at a pre-defined level of, for instance, 1 % below the lowest observed price of the benchmark competitors monitored by the software.

(553) There are several ways increased transparency and the use of price monitoring and pricing software by both retailers and manufacturers may impact the competitive process in e-commerce markets.

(554) First, increased price transparency through price monitoring software enables easier detection of those retailers that deviate from manufacturers' pricing recommendations. It could therefore allow manufacturers to retaliate against retailers that do not comply with pricing recommendations.³⁰⁷ It may even limit the incentives of retailers to deviate from such pricing recommendations in the first place.

(555) Second, increased price transparency through price monitoring software may facilitate or strengthen (both tacit and explicit) collusion between retailers by making the detection of deviations from the collusive agreement easier and more immediate. This, in turn, could reduce the incentive of retailers to deviate from the collusive price by limiting the expected gains from such deviation.³⁰⁸

Summary

At least a third of the retailers in each product category receive some form of price recommendations from the manufacturers. The highest proportion of retailers that do so are those active in clothing and shoes, followed by those selling sports equipment and then consumer electronics. Compliance with those indications varies across retailers.

Manufacturers explain that the price of a product is the most immediate way to communicate its quality and intended brand positioning to both retailers and customers. Recommended resale prices are also perceived useful in relation to developing a marketing strategy and supporting the brick and mortar channel.

Most manufacturers track retail prices. Nearly 30 % of them do so systematically. Others track in a targeted manner focussing on certain products, key markets. 67 % of the respondent manufacturers use manual tracking, while nearly 40 % make (also) use of price-tracking software.

Retailers also monitor competitors' prices. The majority of those retailers that use software to do so consequently adjust their own prices to those of their competitors (78 %). Most of them adjust prices manually (43 %), but some (8 %) use automatic price adjustments based on pricing software programmes and a significant share (27 %) uses both manual and automatic price adjustments.

³⁰⁷ Manufacturers could not only intervene based on their own initiative but also following complaints by other retailers about the price level of certain retailers in the market.

³⁰⁸ See also the joint publication by the French and German Competition Authorities, p. 14-15. Available at the following address:
http://www.bundeskartellamt.de/SharedDocs/Publikation/DE/Berichte/Big%20Data%20Papier.pdf?__blob=publicationFile&v=2

Increased transparency and the use of price monitoring/pricing software by both retailers and manufacturers may impact the competitive process in e-commerce markets.

First, it is now easier to detect deviations from manufacturers' pricing recommendations. This could allow manufacturers to retaliate against those deviations. It may even limit the incentives of retailers to deviate from such pricing recommendations in the first place. Second, increased price transparency may facilitate or strengthen collusion between retailers by making the detection of deviations from the collusive agreement easier. This, in turn, would reduce the incentive of retailers to deviate from the collusive price by limiting the expected gains from such deviation.

Several manufacturers emphasise the market position of certain large retailers / groups of retailers. This is reflected, amongst others, in contractually agreed or ad hoc negotiated forms of compensation for retailers' margin losses which shift, at least to a certain extent, the commercial risk back to the supplier.

Manufacturers often voice their intention to create a level-playing field for the different sales online/offline channels taking into consideration the differences in cost levels. Setting different wholesale prices is rarely considered as a viable option due to the risk that a dual pricing strategy could be in breach of Article 101(1) TFEU.

Certain pricing arrangements between manufacturers and their retailers may merit further investigation on a case-by-case basis.

4.7 Exclusivity and parity agreements between retailers and marketplaces and/or price comparison tools

(556) The sector inquiry was also seeking to establish whether agreements between retailers and online marketplaces and/or price comparison tools contain exclusivity and/or parity clauses.

(557) The term "exclusivity clauses" refers to clauses whereby either marketplaces or price comparison tools are restricted from entering into contractual relationships with other retailers (selling the same products) than the contracting one or whereby retailers are restricted from selling on other marketplaces or listing their products on other price comparison tools.

(558) Parity clauses (often referred to as most-favoured-nation clauses or "MFNs") typically require the retailer to sell on the marketplace or list on a price comparison tool at the lowest price and/or on the best terms offered either on retailer's own website (narrow parity clauses) or on other marketplaces/price comparison tools or in all sales channels (wide parity clauses). Non-price parity clauses may for instance require the retailer to offer the same (or a not narrower) product range on the marketplace (and/or price comparison tool) than on its own website, or require similar customer services.

4.7.1 Agreements between retailers and marketplaces

- (559) Based on the preliminary results of the sector inquiry, exclusivity clauses between marketplaces and retailers selling on the marketplace are rare. None of the marketplaces participating in the sector inquiry reported to have agreements with retailers that require them to exclude other retailers that offer the same products from the marketplace. Only one marketplace reported that it requires retailers not to sell some or all of their products on other marketplaces or other websites.
- (560) Unlike exclusivity clauses, parity clauses are slightly more present in the agreements between retailers and marketplaces. The data from the sector inquiry suggest that those marketplaces that use parity clauses are either more sizable or are new entrants. Typically used parity requirements are the ones that request the retailers to sell on the marketplace at a price that is lower or at most equal to the lowest price offered by the retailer on any other marketplace (used by 8 of the respondent marketplaces) and those that request the retailer to offer on the marketplace the same product range as elsewhere, for example on other marketplaces, websites and brick-and-mortar shops (also used by 8 of the respondent marketplaces).
- (561) Most marketplaces using the above-described wide price parity clauses are not identical to the ones using the product range parity clauses. Most of those marketplaces that use wide price parity clauses (6 out of the 8 using wide price parity clauses) also use narrow ones which require retailers to sell on their marketplace at a price that is lower or at most equal to the lowest price available on the retailer's own website. Only one marketplace reported to use price parity clauses that require retailers to sell on the marketplace at lower or equal price compared to the price applied in their brick and mortar shop.
- (562) The preliminary findings suggest that parity clauses which are used by the respondent marketplaces are not limited to price and product range. Under some clauses retailers are required to ensure that the level of quality of the customer service and the product information provided to the potential buyers shall not be worse than those offered by the same retailer in other sales channels. None of the marketplaces reported to have parity clauses with respect to product quality.
- (563) 43 % of respondent marketplaces (22 respondents) reported not to have any parity requirements in their agreements and several marketplaces apply parity requirements only with respect to their most important retailers. Some of the marketplaces have pointed out that despite the existence of parity clauses in their agreements with retailers, the latter are not enforced and some of them have been removed. The preliminary findings suggest that parity clauses tend to be present in agreements with larger marketplaces.
- (564) Among the respondent retailers only a few reported to have price parity requirements in their agreements with marketplaces. 2 % of the retailers that responded to the questionnaire have a pricing restriction with regard to at least one product category,

whereby the retail price on a marketplace cannot be higher than the one on retailer's website (narrow parity clause). Similarly, 2 % of retailers have a pricing restriction with regard to at least one product category, whereby the retail price on a given marketplace cannot be higher than the one on other marketplaces (wide parity clause).

- (565) As to the reasons why parity clauses are applied marketplaces explained that having a broad and recent range of the retailers' products (ensured by product range parity clauses) is necessary to build and maintain customer trust. Others claim that parity clauses are important to compensate for the investment of the marketplace to integrate the retailers' products into their system. There are also marketplaces whose business model is based on being a bargain superstore which implies having the lowest price on the market. As one of the marketplaces explains, "[...] *Majority of online shoppers feel that price is one major factor for a purchasing decision. Therefore it is important to have sellers who offer their products at least for a competitive price with respect to different marketplaces.*"
- (566) Some marketplaces monitor the compliance with parity clauses regularly, whereas others do it from time to time only. In case of non-compliance, marketplaces first warn the retailers and as an ultimate step they exclude them from the relevant seller-scheme or from the marketplace.
- (567) When asked about the overall impact of the use of parity requirements by other marketplaces, most marketplaces responded that they have not carried out an in-depth analysis of such an impact. A few explain that they have observed a slowdown in their growth after some of the big competitors started to apply price parity clauses. Others claim that their strategy is not to compete with other marketplaces primarily on price but rather on other factors, such as customer service, quality, efficiency of logistics, or availability of the latest products.
- (568) In the absence of a hardcore restriction under Article 4 of the Vertical Block Exemption Regulation, parity clauses in vertical agreements are covered by the Vertical Block Exemption Regulation if the parties' market shares do not exceed 30 %. Should market shares exceed 30 % an individual assessment of parity clauses will be required.
- (569) In markets where marketplaces play an important role, parity clauses can provide disincentives for retailers to compete on those parameters which fall within the scope of the clause. This may ultimately lead to a reduction of intra-brand competition. Parity clauses may also reduce competition between online retailers and marketplaces and make market entry or expansion for competing marketplaces more difficult.
- (570) Parity clauses may on the other hand lead to efficiencies. For instance their use might be necessary to recoup investments by the marketplace and to avoid free-riding. They may also be used by new market entrants whose business model is based on having the best available resale prices or the widest product range. Parity clauses will therefore have to be analysed and assessed on a case-by-case basis.

4.7.2 Agreements between retailers and price comparison tools

(571) All price comparison tool providers but one declared that they do not have any contracts with retailers on an exclusive basis, meaning retailers using price comparison tools are free to contract with competing ones.

(572) According to the preliminary findings of the sector inquiry, agreements between retailers and price-comparison tools containing price parity clauses are exceptional. Only 3 % of the respondent price-comparison tools reported to have such clauses in their agreements.

(573) According to these parity clauses, prices displayed on the price comparison tool have to be lower or at most equal to the lowest price offered by the same retailers on other price comparison tools, on any marketplace, on their own website or in their brick-and mortar shop. However, price comparison tools claim that these parity clauses are not enforced.

Summary

According to the preliminary findings of the sector inquiry, exclusivity clauses between marketplaces/price comparison tools and retailers selling on the marketplace are exceptional. Parity clauses (both price and non-price ones) are more present in particular in agreements between retailers and larger marketplaces. Only 2 % of the respondent retailers have a parity clause with regard to at least one product category.

In markets where marketplaces play an important role, parity clauses can provide disincentives for retailers to compete on those parameters which fall within the scope of the clause. This may ultimately lead to a reduction of intra-brand competition. Parity clauses may also reduce competition between online retailers and marketplaces and make market entry or expansion for competing marketplaces more difficult. Parity clauses may on the other hand lead to efficiencies. For instance their use might be necessary to recoup investments by the marketplace and to avoid free-riding. Parity clauses will therefore have to be analysed and assessed on a case-by-case basis.

4.8 Other types of restrictions to sell or advertise online

(574) The restrictions described above are contractual restrictions on which the Commission has requested more detailed information from market participants. They do however not constitute an exhaustive list of restrictions encountered in the sector inquiry. Moreover, new developments in e-commerce markets may lead to new types of contractual restrictions which may require closer scrutiny in the future.

(575) Many manufacturers include a significant number of detailed clauses in their distribution agreements on how their products can be sold and advertised online. This is

in particular the case for selective distribution agreements.³⁰⁹ Such clauses relate for example to:

- (a) technical requirements for the website (e.g. availability of website and rapidity);
- (b) requirements in relation to the design of the website (e.g. allowing clear and easy navigation) and the display of the products on the website;
- (c) requirements to provide certain (pre- and post-sale) customer services and adhere to certain service requirements;
- (d) adherence to brand policy requirements of the manufacturer; and
- (e) requirements in relation to delivery and immediate availability of stock.

(576) These clauses typically aim at guaranteeing certain quality standards in relation to online distribution of the manufacturers' products by (authorized) retailers.

(577) Other types of clauses include restrictions that may dissuade (authorized) retailers from using the internet to reach a greater number and variety of customers by imposing criteria for online sales which are overall not equivalent to criteria imposed for the sales from the brick and mortar shops³¹⁰ or for contractual provisions which restrict internet sales per se.³¹¹

(578) The information obtained in the sector inquiry shows that a limited number of retailers are restricted in their ability to sell (some) products of certain manufacturers via the internet at all. In this context, it should be recalled that contractual provisions which either explicitly or de facto prohibit a retailer to use the internet as a method of marketing are restrictions by object under Article 101(1) TFEU and hardcore restrictions within the meaning of Article 4(b) and 4(c)³¹² of the Vertical Block Exemption Regulation. Such clauses cannot be regarded as prohibiting members of a selective distribution system from operating out of an unauthorised place of establishment within the meaning of Article 4(c) of the Vertical Block Exemption Regulation and could only escape the prohibition of Article 101 TFEU on an individual basis where the conditions of Article 101(3) TFEU are met.³¹³

(579) Another type of restriction encountered in the sector inquiry relates to the use of trademarks/brand names for online advertising. Some contractual clauses limit the ability of (authorized) retailers to use the manufacturers' (trademark protected) brand

³⁰⁹ See section B.3.4.3 *Selective distribution* on selective distribution.

³¹⁰ Vertical Guidelines paragraph 56.

³¹¹ Judgment in *Pierre Fabre Dermo-Cosmétique SAS vs. Président de l'Autorité de la concurrence* EU:C:2011:649.

³¹² See judgment in *Pierre Fabre Dermo-Cosmétique SAS vs. Président de l'Autorité de la concurrence* EU:C:2011:649, paragraphs 53 et seq and Vertical Guidelines paragraph 52.

³¹³ Judgment in *Pierre Fabre Dermo-Cosmétique SAS vs. Président de l'Autorité de la concurrence* EU:C:2011:649, paragraphs 56 and 59.

names for online marketing or optimization activities irrespective of whether such usage could amount to a trademark violation and even insofar as such usage would be allowed under trademark rules.³¹⁴

(580) The preliminary results of the sector inquiry suggest that some retailers are limited in their ability to use or bid on the trademarks of certain manufacturers in order to get a preferential listing on the search engines paid referencing service (such as Google Adwords) or are only allowed to bid on certain positions. Such restrictions typically aim at preventing retailer's websites from appearing prominently in the case of usage of specific keywords. This may be in the interest of the manufacturer in order to allow its own retail activities to benefit from a top listing and keep bidding prices down. Given the importance of search engines for attracting customers to the retailers' website and improving the findability of their online offer, such restrictions may also raise concerns under Article 101 TFEU as they restrict the ability of retailers to attract online customers. Conversely, restrictions on the ability of retailers to use the trademark/brand name of the manufacturer in the retailer's own domain name rather help avoiding confusion with the manufacturer's website.

Summary

New developments in e-commerce markets may lead to new types of contractual restrictions which may require closer scrutiny in the future.

Many manufacturers include a significant number of detailed clauses in their distribution agreements on how their products can be sold and advertised online. This is in particular the case for selective distribution agreements.

There are also other restrictions that may aim at dissuading retailers from using the internet as a means to reach more customers. In this respect, it should be recalled that absolute internet bans are hardcore restrictions. They fall outside the Vertical Block Exemption Regulation and escape Article 101 TFEU only if they can be justified under Article 101(3) TFEU. Finally, restrictions on the use of trademarks for advertisement purposes may also raise concerns under Article 101 TFEU.

³¹⁴ See judgment in *Google France and Google*, C-236/08 to 238/08, EU:C:2010:159, paragraphs 75 et seq.

5. OTHER OBSERVATIONS

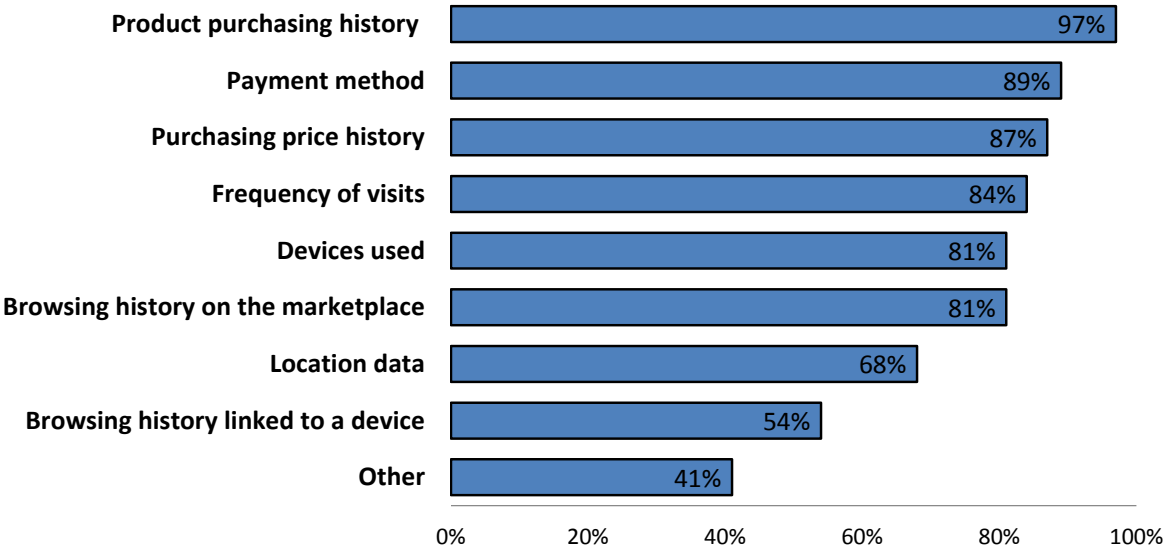
5.1 Customer data

(581) The questionnaires addressed to marketplaces and price comparison tools gathered some information about the collection and use of such data.

(582) Whereas all marketplaces participating in the sector inquiry report collecting individual customer data, 77 % of the price comparison tool providers do so.

(583) Marketplaces collect a wide range of different data such as location; product, price, purchasing and browsing history; frequency of visits; the devices and payment methods used.

Figure B. 77: Proportion of marketplaces collecting each type of data³¹⁵

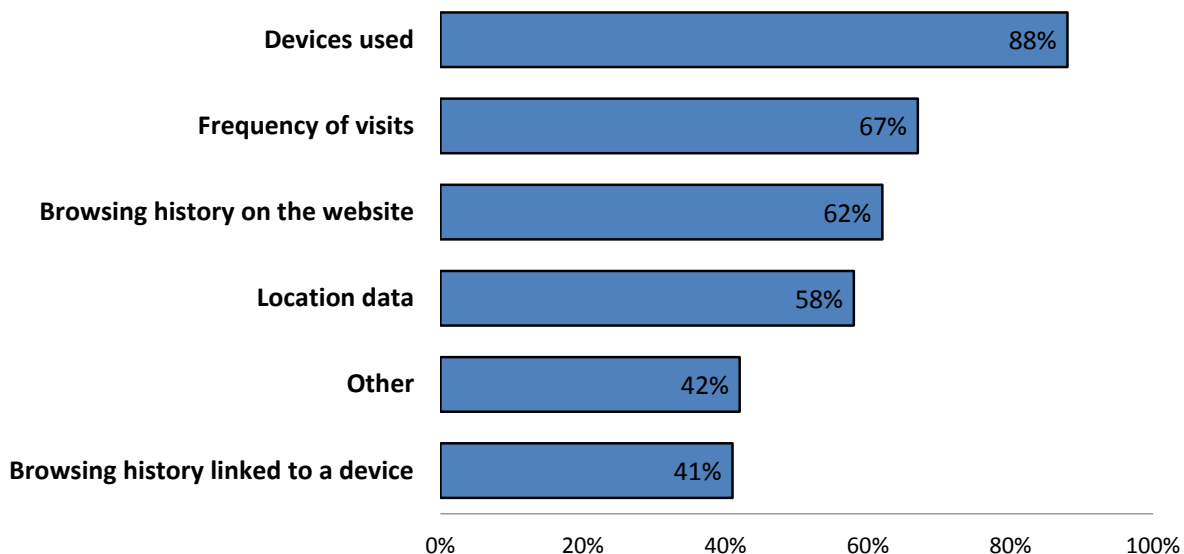


(584) Besides the data listed above, marketplaces also collect personal identification data (such as name, mother's name, age), contact details (including physical and mail address, phone number), electronic identification data (such as device ID's), customer profile data (preferences, habits, chats, languages, interests, profiles), financial information (including billing, bank account number, and payments system data) and feedback data.

(585) Price comparison tools also collect different types of data, most typically concerning the device used by the customer.

³¹⁵ All 37 respondent marketplaces responded to the question.

Figure B. 78: Proportion of price comparison tools collecting each type of data³¹⁶



(586) Besides the data listed above, few of the respondent price comparison tools also collect personal identification data and contact details about different categories of customers, (such as registered and past customers, customers from trusted reviews programme) as well as electronic identification data. Some also explain to collect anonymized data, not connected to individuals. Price comparison tools also collect and use third party analytics data (such as keywords, traffic sources, operating systems, browsers and devices used).

(587) Marketplaces and price comparison tools use part of the collected data to invoice retailers. As some respondents explain, they distinguish via the collected data the human clicks from software (internet bot) ones. Some price comparison tools explain that they charge different prices for clicks from foreign and from domestic IP addresses. A few explain that they also charge different prices for clicks from mobile and desktop devices due to different conversion rates. Some identify repeated clicks (within a short timeframe) from the same IP, so as to avoid charging the seller inadequately.

(588) Marketplaces and price comparison tools use part of the collected data to improve customer experience. For instance browsing history allows for customers to see the products visited earlier. Displays may also be adapted to device types. For instance when browsing from smartphone, some price comparison tools only expose merchants who provide a smartphone-optimized experience.

(589) They also use the collected data to assess and improve business performance. With the help of the collected data they analyse customer behaviour and demand (such as the number of unique and frequent customers, the reaction to promotions, to prioritize features that may be more popular in a certain geolocation; optimise product listings and

³¹⁶ 69 price comparison tools responded to the question.

displays (as search algorithm "learns" from past history); improve marketing activity (for instance to display personalised banners); and develop the service provided as well as their website.

- (590) Finally, they also use the data for security and fraud prevention and to comply with legal and accounting obligations.
- (591) Roughly half of the marketplaces share some data with their professional sellers whose product was visited or purchased. Those marketplaces that do so typically provide the data necessary to process the transaction and their own individual sales data and analytics. Roughly one-quarter of price comparison tools reported to share data (typically click data and information on the devices used) with the sellers whose products were visited.
- (592) Marketplaces and price comparison tools typically do not sell data to third parties. The few that do so sell them to research companies and advertisers.
- (593) One-third of the marketplaces and few price comparison tools report to purchase data from third parties. If they do so, they purchase from entities which offer credit check and identity check services; anonymous and aggregated data from market research companies and institutions; media companies; and also personal identification data from marketing companies.
- (594) Retailers also collect data for other than geo-blocking purposes (as discussed in more detail in section B.4.3.2.5). They report to gather a considerable amount of both personal data (linked to the individual customers)³¹⁷ and "big data" (for instance click) data. The most typical data collected are: the customers' physical address (in particular post code), real location (e.g. GPS coordinates, Wlan-data, IP address) delivery address, billing address, email address, phone number; name, birth date, gender, language, credit card and banking data, customer communication, PC information, the browser used, and data on visit- search- and purchase history.
- (595) The purpose of the data gathering is diverse. For obvious reasons the same information can be used for different purposes. For instance the billing address might be used for both communicating the bill to the customer and to send him newsletters). The most typical purposes mentioned are the following: completion of delivery and managing delivery-relating communication; executing the payment transaction; fulfilling after-sales services; payment verification and fraud prevention; bots' fraud screening;

³¹⁷ Personal data is defined in Article 2(a) of the Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995 on the protection of individuals with regard to the processing of personal data and on the free movement of such data as mean any information relating to an identified or identifiable natural person ('data subject'); an identifiable person is one who can be identified, directly or indirectly, in particular by reference to an identification number or to one or more factors specific to his physical, physiological, mental, economic, cultural or social identity. Directive 95/46/EC will be replaced by the Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data. It entered into force on 24 May 2016, providing for analogous definition of personal data. It will be applicable as of 25 May 2018.

preventing website hacking; managing customer relations; marketing; carrying out performance analytics; compliance with different laws in the Member States (for instance to comply with different VAT-rates or consumer protection laws).

Summary

All marketplaces and the majority of price comparison tools collect data for different purposes. Retailers also gather a considerable amount of both personal and anonymous data. Data are mostly used to complete and invoice transactions, for marketing, to improve business performance, to prevent fraud and to comply with legal obligations.

C. E-COMMERCE IN DIGITAL CONTENT

(596) Digital content that is protected by copyright law, similar to other copyright-protected works, does not enjoy unitary protection in the EU. Instead, national copyright laws are applicable in each of the 28 Member States.³¹⁸ Copyright protection is "territorial" in the sense that exclusive rights are enforced under the national laws of each Member State.

(597) In order to provide online services that include copyright protected content, a digital content provider must generally obtain a licence from the holders of the copyrights in such content, such as film producers or record labels. Rights in broadcasts of sports events are licensed in a similar way, as in some Member States such broadcasts also benefit from certain protection under the national copyright laws.

(598) With respect to digital content, the sector inquiry aims at identifying potential contractual restrictions originating from the contractual relationships between suppliers (right holders) and providers of online digital content services (licensees).

1. CHARACTERISTICS OF RESPONDENTS

1.1 Digital content providers

1.1.1 Types of operators

(599) While operators were asked to describe their activities, the markets in which they operate, and their competitors, they were not asked to categorise their business model.

(600) However, for the purposes of this Preliminary Report, the Commission has sought to identify the principal activity of operations ("type of operator") and the main business model ("business model") of the respondents. While such definitions have the benefit of simplicity, they are necessarily imprecise. A sizeable proportion of respondents might fall within more than one definition.

(601) The following definitions were used in relation to the type of operators:

- (a) **Public service broadcaster:** A broadcaster which is funded mainly, if not fully, through public funds, including regional broadcasters;
- (b) **Commercial broadcaster:** A private sector broadcaster which is funded primarily through non-public funds, typically through advertising revenues raised by selling slots during programmes;

³¹⁸ National copyright laws are however harmonised to a large extent by several EU Directives, such as Directive 2001/29/EC of the European Parliament and of the Council of 22 May 2001 on the harmonisation of certain aspects of copyright and related rights in the information society; Directive 2014/26/EU of the European Parliament and of the Council of 26 February 2014 on collective management of copyright and related rights and multi-territorial licensing of rights in musical works for online use in the internal market; Directive 2006/115/EC of the European Parliament and of the Council of 12 December 2006 on rental right and lending right and on certain rights related to copyright in the field of intellectual property, and Directive 2011/77/EU of the European Parliament and of the Council of 27 September 2011 amending Directive 2006/116/EC on the term of protection of copyright and certain related rights.

- (c) **Online audiovisual operator:** Any other type of broadcaster or operator providing music or audiovisual content, in part or in full doing so through online services (including paid services, both transaction- and subscription-based, and free online services);
- (d) **Fixed line PSTN and cable operators:** An electronic communications operator using a traditional switched telephone network ("PSTN") or a cable network ("cable"), and which also provides digital content as part of its offer;
- (e) **Mobile operator:** An electronic communications operator using a mobile network, and which also provides digital content as part of its offer;
- (f) **Portal/Web TV operator:** An operator of an internet portal or channel offered online;
- (g) **Publisher:** An operator which is predominantly operating in the print media sector and which also offers digital content online; and
- (h) **Other:** Any operator not fitting into any of the categories listed above.

(602) Table C. 1 provides the proportion of each of the categories above in the sample of respondents.

Table C. 1: Digital content provider respondents classified according to type of operation

Type of operator	Number of respondents	Proportion in sample
Commercial broadcaster	79	28%
Online audiovisual operator	53	19%
Public service broadcaster	50	18%
Fixed line PSTN operator	21	8%
Portal / Web TV	17	6%
Fixed line cable operator	17	6%
Publisher	16	6%
Mobile operator	15	5%
Other	10	4%
Total	278	100%

1.1.2 Business models

(603) A broad spectrum of revenue generating business models of digital content providers are covered by the sector inquiry. As in the previous section, the definitions are necessarily imprecise.³¹⁹

(604) The following definitions of categories of business models are used for the purposes of the sector inquiry:

³¹⁹ Several respondents have business models which fall within more than one of the categories used. In this case, the type of business model chosen is the one that appears to be the predominant one or the original one.

- (a) **Publicly funded:** An operator which receives most of its revenues from public funds;
- (b) **Advertising-funded:** An operator which receives most of its revenues from selling advertising space or time;
- (c) **Subscription-based:** An operator which receives most of its revenues from selling services for a subscription fee;
- (d) **Transaction-based:** An operator which receives most of its revenues from selling services on the basis of individual payments for each item accessed;
- (e) **Packager of content:** An operator which earns most of its revenues on the basis of licensing fees from channels or otherwise packaged content to other digital content providers. These operators provide digital content services directly to users only as a small part of their activities;
- (f) **Hosting online operator / device:** An operator which derives most of its revenues from sales of hosting software / devices, or from agreements with digital content providers (e.g. a revenue-sharing agreement) selling their services to users via hosted software programmes (e.g. applications or "apps", or channels), or from advertising, or from a combination of all these elements. The hosting environment can be created through online applications, such as video portals (e.g. YouTube), or through hardware devices, such as online video streamers (e.g. Roku).
- (g) **Other:** An operator which does not fit in any of the categories above.

(605) Table C. 2 provides the proportion of each of the categories above in the sample of respondents.

Table C. 2: Digital content provider respondents classified according to business model

Type of business model	Number of respondents	Proportion in sample
Advertising-funded	77	28%
Subscription-based	78	28%
Publicly funded	49	18%
Packager of own content	36	13%
Transaction-based	21	8%
Other	7	3%
Hosting online operator	6	2%
Hosting device	4	1%
Total	278	100%

1.1.3 Size of activities

(606) Digital content provider respondents include different businesses, in terms of overall turnover³²⁰:

- (a) Very large companies: annual revenues above EUR 500 million;
- (b) Large companies: annual revenues between EUR 10 million and 500 million;
- (c) Medium companies: annual revenues between EUR 500 000 and 10 million; and
- (d) Small companies: annual revenues below EUR 500 000.

(607) Table C. 3 provides the average worldwide turnover of respondents in each category. Table C. 4 then provides the average proportion of turnover from online activities in relation to worldwide turnover. Both tables also provide the number of respondents in each category.

Table C. 3: Average turnover of digital content providers by size and by year (million EUR)

Category	Number of companies	2010	2011	2012	2013	2014
Very large	59	3,545.70	3,548.02	3,534.95	3,444.42	3,584.23
Large	101	144.78	144.04	134.47	141.69	120.46
Medium	61	4.50	4.63	4.68	3.92	3.42
Small	32	0.25	0.18	0.17	0.17	0.17
Total	253	1,042.20	971.99	940.30	897.49	887.03

Table C. 4: Online turnover as a proportion of total turnover for digital content providers, average by size and by year

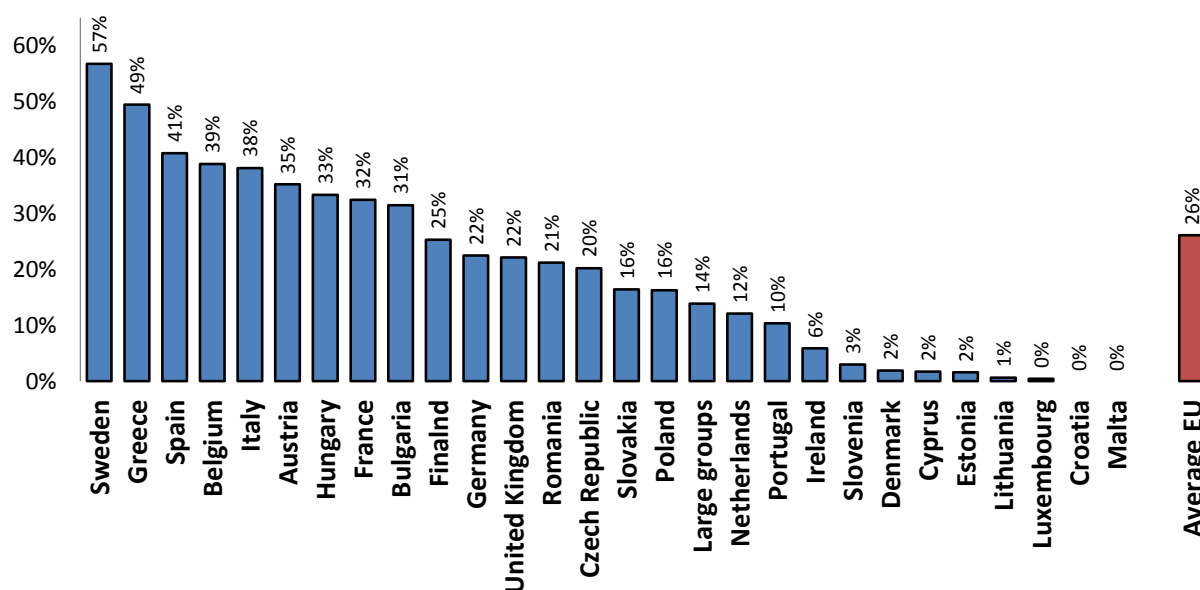
Category	Number of companies	2010	2011	2012	2013	2014
Very large	59	9%	10%	12%	12%	10%
Large	101	15%	18%	16%	17%	19%
Medium	61	40%	41%	41%	41%	38%
Small	32	55%	43%	51%	50%	56%
Total	253	23%	25%	26%	26%	26%

(608) The sector inquiry thus covers companies with worldwide turnovers ranging from less than EUR 1 000 to more than EUR 39 billion in 2014. Overall, digital content provider respondents generate about 26 % of their overall turnover from online activities. This percentage tends to grow as the size of the company decreases.

(609) Figure C. 1 shows the distribution of respondents by Member State, ranked in decreasing order of importance of online turnover as a proportion of overall turnover.

³²⁰ A smaller sample of 253 respondents provided adequate information on turnover. The respondents providing partial or inaccurate information were excluded from the tables in this section.

Figure C. 1: Online turnover as a proportion of total turnover for digital content providers, average by Member State in 2014



1.1.4 Revenue breakdown and advertising revenues

(610) Digital content service providers were asked to provide a breakdown of their revenues stemming directly from the distribution of content, both online and non-online, for the year 2014. Table C. 5 provides the proportions of revenues generated by digital content providers for each of several activities.³²¹

Table C. 5: Proportion of total revenues generated through different channels for all digital content providers in 2014

Online sub- scription	Non- online sub- scriptions	Online trans- actional	Non- online trans- actional	Online advertising	Non- online advertising	Other online	Other non- online	Public subsidy
26%	14%	15%	8%	17%	11%	2%	4%	2%

(611) Online distribution of content represents a significant part of business for the respondent digital content providers. Among the potential revenue sources, the sale of advertising slots either online (i.e. as banners or equivalent) or within the digital content provided (as a "standard" advertising slot within a programme) is an important revenue stream for more than a third of respondents (Figure C. 2). Such revenues are particularly important for more than half of publishers and commercial broadcasters offering digital content services, but this revenue stream is also important for portals / Web TV operators and for online audiovisual operators (Figure C. 3).

³²¹ Subscription, transactional, advertising and subsidies are used in this section with the same meaning as in section C.1.1.3 *Size of activities*.

Figure C. 2: Proportion of all digital content providers generating advertising revenues

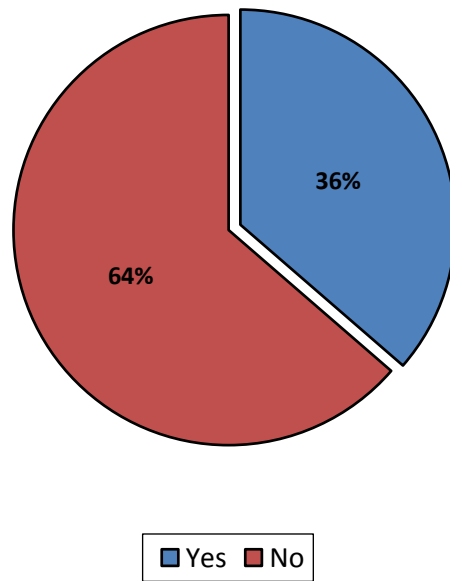
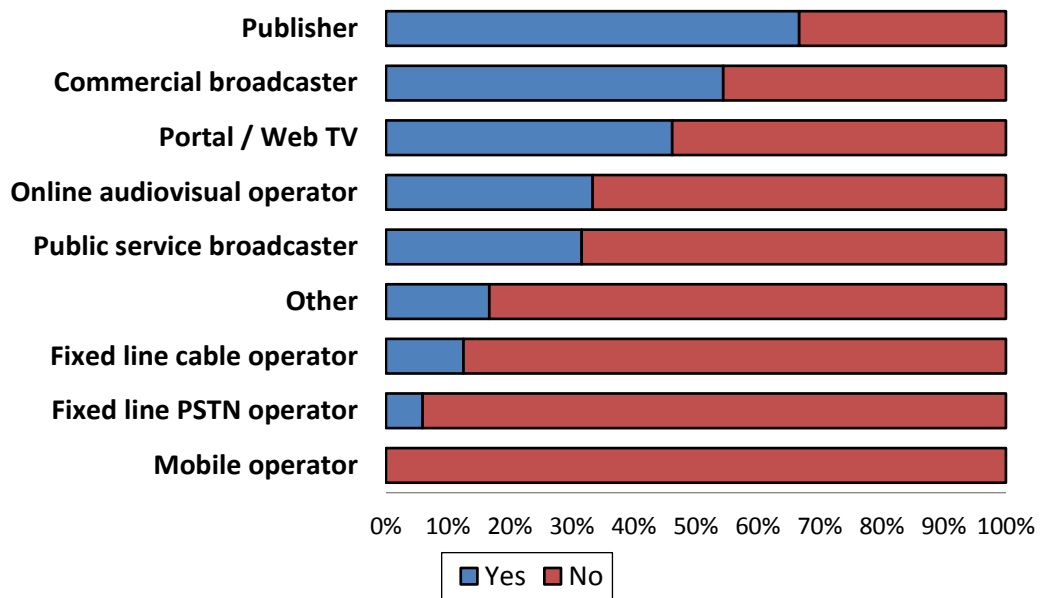
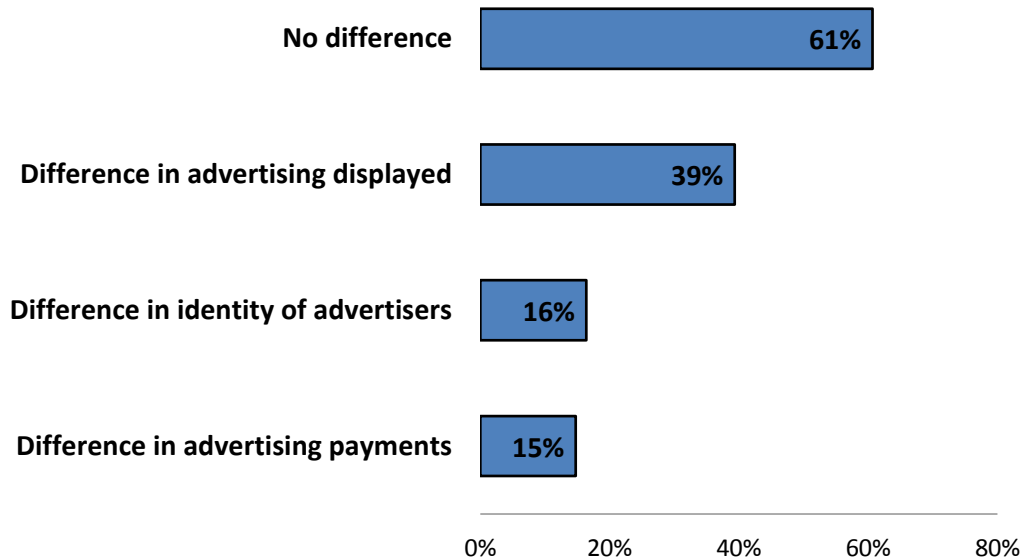


Figure C. 3: Proportion of digital content providers generating advertising revenues by type of operator



(612) Respondents generating advertising revenues were asked to specify whether they adopted different strategies depending on the Member States where they operate (Figure C. 4).

Figure C. 4: Proportion of digital content providers adopting different advertising strategies in different Member States



(613) The figure shows a relatively high degree of location-specific differentiation in advertising. Even though the identity of advertisers does not differ for most respondents, almost 40 % indicate advertisement content changes depending on the Member State. This proportion is particularly high for commercial broadcasters (52 % of respondents change the advertisements displayed) and publishers (50 %).

1.2 Right holders

1.2.1 Types of right holders

(614) Respondent right holders include both smaller / national operators along with a number of players with a significant cross-border / international presence, and new entrants as well as established operators. In particular, three main categories of respondents can be identified:

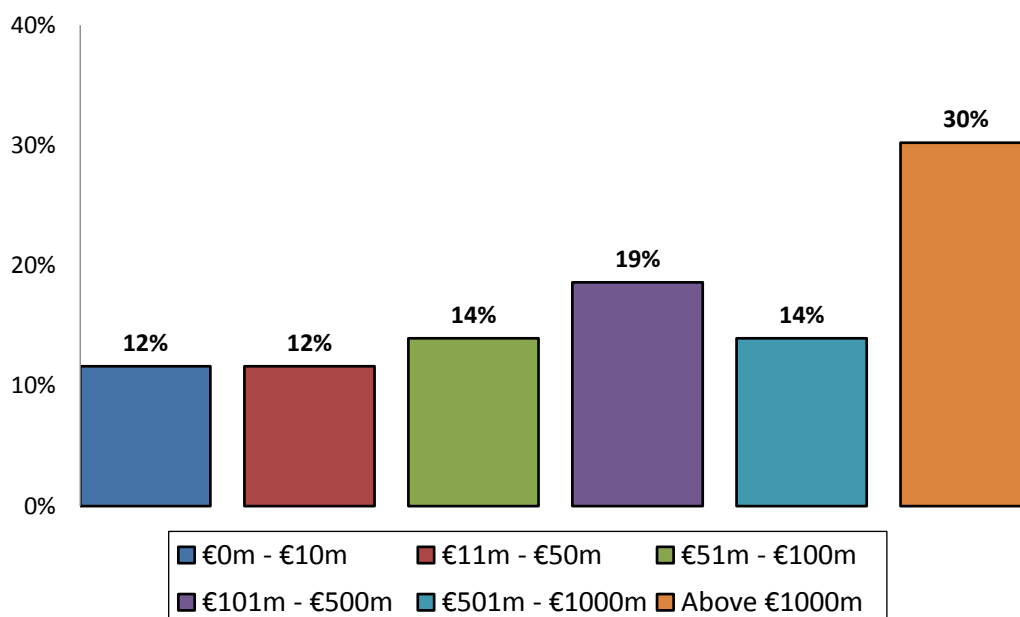
- (a) Rights holders that are active in the production of digital content;
- (b) Media agencies, i.e. intermediaries in charge of the commercial exploitation of rights which have been licensed to them by right holders; and
- (c) Vertically-integrated right holders, active both upstream as producers of content, and downstream as providers of digital content to consumers.

1.2.2 Size of activities of right holders

(615) As follows from Table A. 3 above, 53 right holders submitted information and licensing agreements in reply to the sector inquiry. Forty-four of those respondents submitted data

concerning their global turnover in 2014. As stated above, the questionnaire to right holders was sent to companies and associations of different sizes.³²² This is reflected by the submitted data, which indicate that the global turnover of this type of respondent ranges from less than EUR 10 million to above EUR 1 000 million in 2014. 30 % indicated that their global turnover in 2014 was above EUR 1 000 million. Right holders in fiction and children TV had the highest turnover figures, followed by right holders in sports, and then music.

Figure C. 5: Global turnover figures for 2014 – All right holders (in million EUR)



1.3 Types of content

(616) As part of the sector inquiry, the Commission asked respondents to provide copies of their licensing agreements and to reply to a set of questions aiming at gauging the key terms and conditions of those agreements.

(617) Digital content providers were asked to provide agreements with the 30 most important suppliers (if applicable) for each of identified product categories. Right holders were asked to provide the eight most valuable agreements overall (again, if applicable) for each of the identified product categories. For both categories of respondents, the importance of suppliers or value of agreements was defined on the basis of the total level of payments resulting from the agreement, or payable to the supplier, for the year 2014.

(618) Digital content providers were asked to distinguish between the following categories of products when ranking the importance of their suppliers:

- (a) **Films:** Feature films and motion pictures;

³²² The associations contacted mainly include certain sports leagues and organisations.

- (b) **Sports:** Sports events and sports programmes, including commentaries;
- (c) **Television fiction:** Television comedy, drama and animation series or programmes;
- (d) **Children television:** Television programmes and series aimed at children, excluding feature films;
- (e) **News:** Television news and current affairs programmes and series;
- (f) **Non-fiction television:** Television content other than films, television fiction, children's programmes, news and sports events; and
- (g) **Music:** Recorded music, excluding music contained in audiovisual content such as background music in films and television programmes.

(619) Right holders were asked to distinguish between the following product categories when ranking the value of agreements:

- (a) **Sports:** A sports event, such as a football match, or a set of sports events, such as a football season, which is the object of a broadcast production or productions;
- (b) **Television fiction:** Television series, comedy, drama, or entertainment programmes, excluding feature films;
- (c) **Children television:** Television programmes and series aimed at children, excluding feature films³²³; and
- (d) **Music:** Recorded music, excluding music contained in audiovisual content such as background music in films and television programmes.

Summary

The sector inquiry focuses on the online provision of audio-visual and music products. At the retail level, a total of 278 digital content providers, both national operators in only one Member State, large groups operating in more than one Member State, and hosting operators were questioned. These respondents submitted information in relation to 6 426 licensing agreements covering films, sports, television fiction and non-fiction, children television, news and music products. A total of 53 right holders replied and submitted information in relation to 282 licensing agreements covering television fiction and children television, sports and music products.

³²³ Television fiction and children television programmes were grouped together in the results from the data submitted by right holders.

2. MARKET TRENDS AND LICENSING PRACTICES

(620) The information provided during the sector inquiry suggests that online transmission has changed the way digital content is accessed and consumed by users. This section outlines the main trends observed and discusses the most prevalent licensing practices.

2.1 Market trends in the provision of online digital content services

(621) Online transmission of digital content is providing new business opportunities to both established operators and new entrants. As observed by several respondents to the sector inquiry, it allows for lower transmission costs per user compared to, for example, terrestrial transmission. Online transmission also provides the flexibility and scalability that satellite transmission does not offer.

(622) Online transmission allows digital content providers to create user interfaces that can be accessed on multiple devices in a seamless way and are easily adaptable.

(623) One of the insights emerging from the sector inquiry is that online transmission is fuelling innovation and experimentation in digital content markets, resulting in a variety of service offerings and business models.

2.2. Licensing practices

(624) One of the key determinants for competition in digital content markets is the scope and the availability of the relevant rights for distribution of digital content. The online distribution of digital content at the retail level requires licensing of a minimum set of rights in order to lawfully market the product – typically including the right to transmit via internet, broadband or cable technologies, and to allow users to stream or download the product via a receiving device.

(625) Over time, complex licensing practices have developed. They reflect the desire on the part of right holders to exploit the rights they hold to the fullest extent possible as well as the need for digital content providers to offer attractive content in order to be competitive.

(626) In order to analyse the competitive landscape in digital content markets it is therefore important to understand how rights are commonly licensed. Rights can be split up in different ways and can be licensed, either on an exclusive or a non-exclusive basis, for a certain territory and/or in relation with certain transmission, reception and usage technologies. While there are in principle no predefined ways to split rights or to bundle them, the main distinctions commonly used unsurprisingly reflect the attractiveness and value of the product to which the licence applies.

(627) The preliminary results of the sector suggest that there are three main distinctions in terms of scope of the relevant rights which are commonly used in licensing agreements:

- (a) **Technology and usage rights:** These include the technologies that the digital content providers may lawfully use to transmit the content and allow the user to receive it, including the modalities of access;
- (b) **Release / duration rights:** These refer to the "release window or windows", i.e. the period of time during which the digital content provider is lawfully entitled to offer the product; and
- (c) **Geographic rights:** These relate to the geographic area or areas in which the digital content provider may lawfully offer the product.

(628) Rights may be licensed using any type of combination of the above mentioned distinctions on an exclusive or non-exclusive basis.

(629) While the focus of the sector inquiry is to understand market conditions and business models in relation to online digital content services, the preliminary results of the sector inquiry indicate that the rights for online distribution are often bundled together with other licensed rights. A preliminary finding of the sector inquiry is therefore that the scope of rights actually licensed to distribute digital content services tends to be broader than the minimum set of rights that would be necessary to provide online digital content services, and often encompasses other transmission and access technologies.

(630) Licensing agreements typically do not allow for the unrestricted use of the licensed rights but come with explicit terms and conditions. Contractual restrictions are therefore not the exception but the norm in digital content markets.

3. THE SCOPE OF LICENSED RIGHTS: TECHNOLOGIES

3.1 Definitions and data set

(631) As part of the sector inquiry, the Commission asked respondents to provide copies of their licensing agreements and to reply to a set of questions aiming at identifying the key terms and conditions of those agreements.

(632) Digital content providers were asked to provide agreements for the 30 most important suppliers (if applicable) for each of the product categories covered by the sector inquiry. Right holders were asked to provide the eight (again, if applicable) most valuable agreements overall. For both categories of respondents, the importance of suppliers or value of agreements was defined on the basis of the total level of payments under the agreement for the year 2014.

(633) Through the responses to the questionnaires, the Commission received a unique data set encompassing more than 6 800 licensing agreements from both digital content providers and right holders.

(634) Respondents were asked to define the scope of rights licensed by them, in the case of right holders, or to them, in the case of digital content providers.

(635) For the purposes of this Preliminary Report, the analysis of the technology and usage scope of rights relies on the following categories³²⁴:

- (a) Rights relating to transmission technologies: rights allowing the digital content provider to use specific technologies to transmit the content to the user, whether encrypted or not encrypted, and irrespective of the specific devices that may be used to input the signal into the distribution stream or to receive the signal by the user. Transmission technologies include the following:
- Online transmission: rights allowing any transmission of the content using TCP/IP³²⁵ and/or related switched-packet protocols which are used for communications between computers, servers or networks over the Internet. Agreements indicating "streaming" or "broadband" as transmission modalities were included in this category;
 - Cable transmission: rights allowing any transmission of the content using a signal which is carried by means of cable, wire or other fibre-based network;
 - Fixed telephone network transmission: rights allowing any transmission of the content using a signal which is carried at least partly over a traditional PSTN³²⁶ telephone network;
 - Mobile transmission: rights allowing any transmission of the content using a signal which is carried by means of a mobile telephone network or local wireless networks (e.g. Wi-Fi, Wi-MAX), regardless of the standard or hardware used;
 - Satellite transmission: rights allowing any transmission of the content using a signal which is carried by means of satellites and which can be received by users;
 - Terrestrial transmission: rights allowing any transmission of the content using a signal which is carried by means of terrestrial antennae relaying analogue or digital broadcasting signals at suitable frequency ranges;

³²⁴ The categories used are often they are the result of an interpretation of specific clauses in agreements and are therefore not precise. Nonetheless they can help in making sense of a vast set of information and in identifying patterns, in particular for technology and usage rights, which are often referred to in licensing agreements.

³²⁵ TCP ("Transmission Control Protocol") / IP ("Internet Protocol") were the first networking protocols to communicate over the internet, in particular for exchanging data by providing specification on how it should be structured in packets, addressed, transmitted, routed and received.

³²⁶ PSTN stands for publicly switched telephone network, and is used to refer to traditional copper-based telephone networks (as opposed to, for example, cable networks or fibre-optic networks). Transmission over this type of network typically entails using a "local loop" that is at least partly not upgraded to fibre, i.e. the last part of the line connecting the network to the user's premises is made of copper.

- Unrestricted transmission: rights allowing transmission of the product by any technology,³²⁷ and
 - Other: rights allowing transmission of the product using technologies different from those listed above.
- (b) Rights relating to reception technologies: these rights specify the devices or technologies that the user is allowed to use to access the content. They include the following:
- TV set: rights allowing reception using a standard TV set;
 - IPTV: rights allowing reception using a "connected" TV set, i.e. a TV set capable of receiving and decoding online signals;
 - Hosting/streaming device: rights allowing reception using a hardware device that can stream digital content and/or host proprietary or third party applications that deliver services to users, including access to digital content products,³²⁸
 - Computer: rights allowing reception using computer hardware, including PC desktops and laptops;
 - Tablet: rights allowing reception using a tablet;
 - Proprietary set-top box: rights allowing reception using a proprietary hardware device, typically provided by the digital content provider as part of the service;
 - Unrestricted: rights allowing reception using any device or technology,³²⁹ and
 - Other: rights allowing reception using devices or technologies different from those listed above.
- (c) Ancillary and usage rights: these rights specify the modalities of access by users, or access possibilities offered by digital content providers. They include the following:
- At home use: rights allowing users to access the content at their home premises;

³²⁷ The "unrestricted" category is used together with any other technologies that might be specified in the licensing agreement and does not replace them. For example, if an agreement contains a license covering "all transmission technologies, including online", the rights are registered as covering both "unrestricted" and "online" technologies. This results in combined percentages exceeding 100 %.

³²⁸ Examples of such devices include online media streamers and hosting devices such as Roku, Amazon Fire TV, Chrome TV, Apple TV, and game consoles such as the PlayStation or Xbox.

³²⁹ See footnote 328 for an indication of how the "unrestricted" category was calculated.

- Mobile use: rights allowing users to access the content while mobile, for example through mobile handsets;
- Catch-up use: rights allowing users to record and replay the content, regardless of the frequency or period of access allowed and regardless of the type of recording technology or device;
- Multi-screen use: rights allowing users to access the content simultaneously on more than one device in the same location, regardless of the type of device;
- Multi-home or second device out of home: rights allowing users to access the content simultaneously on more than one device in different locations, regardless of the type of device;
- Download to own / rent: rights allowing users to download the content, for an unlimited or a limited period of time;
- Streaming: rights allowing users to access the content via streaming;
- Pay/free: rights allowing digital content providers to offer the content either with payment, regardless of the type of relationship with the user, or without payment;
- Available on subscription/on demand: rights allowing digital content providers to offer the content on the basis of either a subscription by the user, or a piece-meal payment for each item accessed;
- Encryption required: requiring digital content providers to use encryption technologies when providing the content to users;
- Portability out of home/out of Member State: rights allowing users to port the content out of their home premises, or out of the Member State of residence;
- Business premises: rights allowing digital content providers to offer the content to commercial users in their business premises;
- Unrestricted: rights allowing digital content providers to offer the content without any restriction in relation to the modalities of access by users;³³⁰ and
- Other: rights allowing digital content providers to offer, or users to access, the content on the basis of modalities distinct from those listed above.

³³⁰ See footnote 328 for an indication of how the "unrestricted" category was calculated.

- (636) The analysis of the **temporal scope of rights (i.e. release windows)** is complex, as release windows are defined differently by different right holders and for different types of content. For the purposes of this Preliminary Report, release windows will be presented taking as the starting point the "first release" of each item.
- (637) For content produced for television, this means typically the first broadcast on television in the EU or in a specific Member State, unless the product is first made available in the EU through online distribution, in which case "first release" refers to the first availability through online distribution. For films, the first release is typically the first theatrical release in the EU or in a specific Member State. For sports events, the "first release" is normally the live broadcast of the event.³³¹
- (638) For all types of content, rights relating to release windows will mainly be presented by distinguishing between the different periods of time during which digital content providers are allowed to offer such content. Hence, for example "1 – 30 days" refers to rights that allow digital content providers to offer the content in the period ranging from 1 to 30 days after its first release.
- (639) Finally, the analysis of the **geographic scope of the licensed rights** refers to the Member State(s) in which the rights allow digital content providers to lawfully offer to transmit, and users to receive, the product or service.
- (640) In the preliminary results presented in the following sections, where a figure or table includes certain rights, it means that such rights are among those that have been licensed to the respondents. For example, a table indicating that 80 % of agreements include online transmission must be read as indicating that right holders have licensed online transmission rights to digital content providers in 80 out of 100 agreements.
- (641) The majority of licensing agreements submitted by digital content providers and right holders contain complex definitions of the scope of certain technologies that licensees (i.e. digital content providers) and users are allowed to use. The licensed rights are often split up along different transmission technologies such as satellite, terrestrial, online or mobile; reception technologies such as TV set, computer, tablet; or usage technologies such as streaming or download.
- (642) On the one hand, splitting up rights in order to allow a variety of digital content providers to offer their services by using different technologies may increase competition in digital content markets. On the other hand the granting of exclusive rights for certain transmission technologies such as online may make it more difficult for new entrants, smaller operators, or other market participants to obtain the rights to the service they want to deliver.

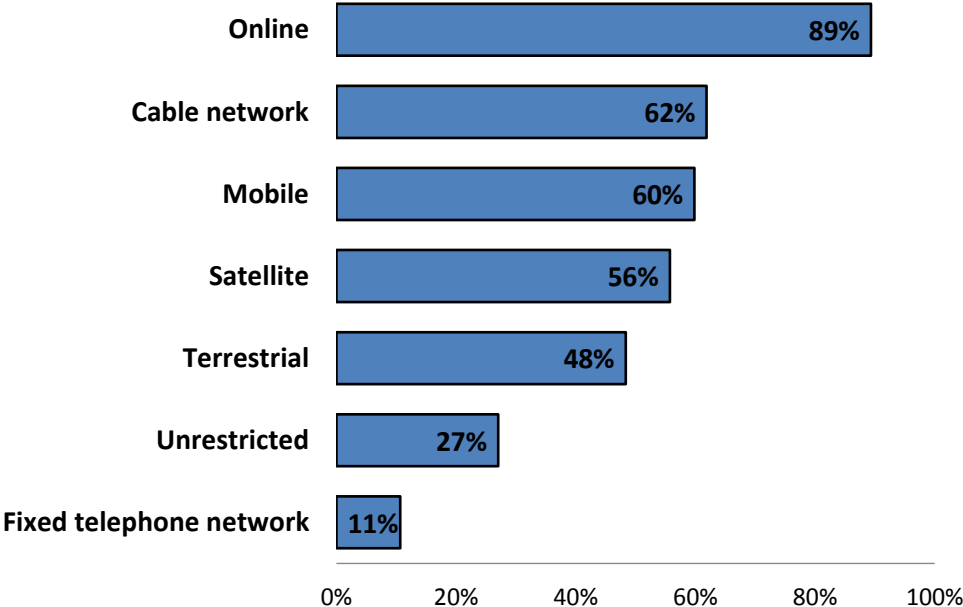
³³¹ These definitions are illustrative and used for the purposes of this Preliminary Report. For example, the simulcast of a product (i.e. simultaneous transmission) using terrestrial, cable and online transmission qualifies as a "first release" for the purposes of this Preliminary Report – and is therefore also referred to as such throughout the text. However, this is a different "first release" window compared to the theatrical release of a film, or the live broadcast of a sports event.

(643) Most licensing agreements specifically define the transmission methods which digital content providers are allowed to use, as licensees of the rights conferred to them.

(644) The majority of the licensing agreements submitted by right holders³³² include specific provisions relating to online transmission or include online transmission among the licensed transmission technologies (see Figure C. 6). Almost 90 % of the examined licensing agreements grant digital content providers to right to offer online the specific content covered by the agreement.

(645) What is interesting about this finding is the fact that online transmission is specifically mentioned in the agreements, which points to its growing importance.

Figure C. 6: Proportion of agreements including specific transmission technology rights – All agreements submitted by right holders



(646) Interestingly, the third most widely mentioned transmission technology in the agreements is mobile transmission. As explained in paragraph (635) above, mobile transmission does not relate solely to mobile telephone networks but any transmission allowing users to access content while being mobile (including, most importantly, on mobile devices used in closed perimeters, such as through Wi-Fi networks). This reflects the increasingly important role of mobile devices in media consumption.

(647) Cable, satellite and terrestrial transmission are the most widely licensed among more traditional transmission technologies.

³³² Respondents were asked to provide the information per agreement with each supplier (right holder). Therefore while at the level of each individual respondent the information obtained is per supplier, over the whole sample, there may be duplication of suppliers across respondents. The results are therefore interpreted based on the number of contractual relationships or agreements.

(648) Only slightly more than a quarter of agreements include unrestricted transmission rights, meaning that they confer to digital content providers the right to use any transmission technology, either explicitly (i.e. by specifying that all transmission technologies are allowed) or implicitly (i.e. by not mentioning any transmission right, thereby not restricting the scope of the rights to a specific transmission technology).

(649) Licensing with regard to specific transmission technologies differs between types of content.

(650) First, for children TV, television fiction and films (Figure C. 7, Figure C. 8, Figure C. 9, respectively) licensed transmission technologies are in most cases explicitly defined, and they tend to include a high proportion of online, mobile and terrestrial technologies.

Figure C. 7: Proportion of agreements including specific transmission technology rights – Children TV agreements submitted by digital content providers

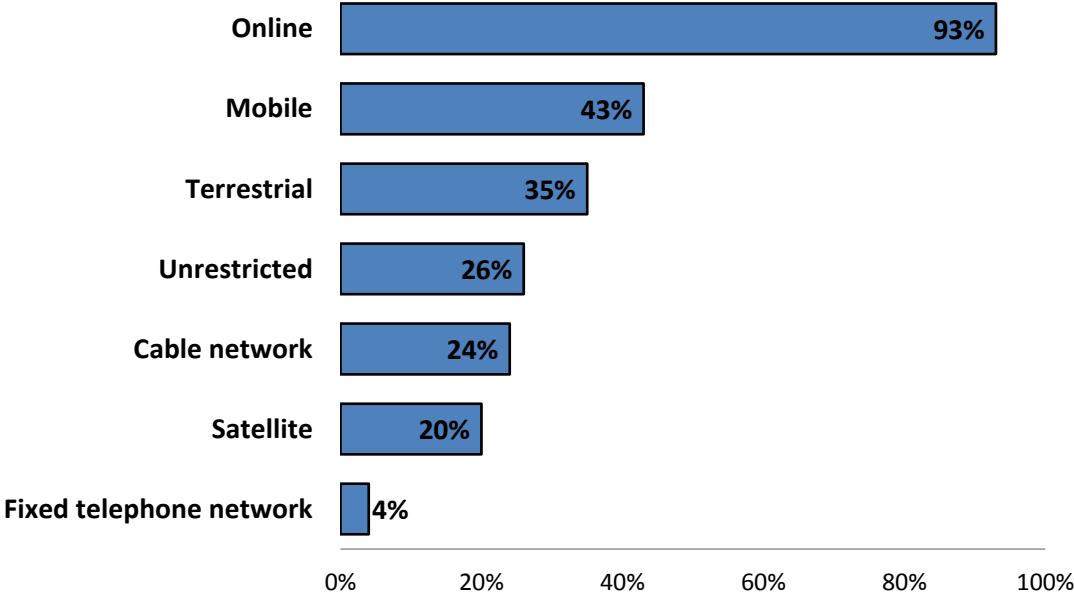


Figure C. 8: Proportion of agreements including specific transmission technology rights – Television fiction agreements submitted by digital content providers

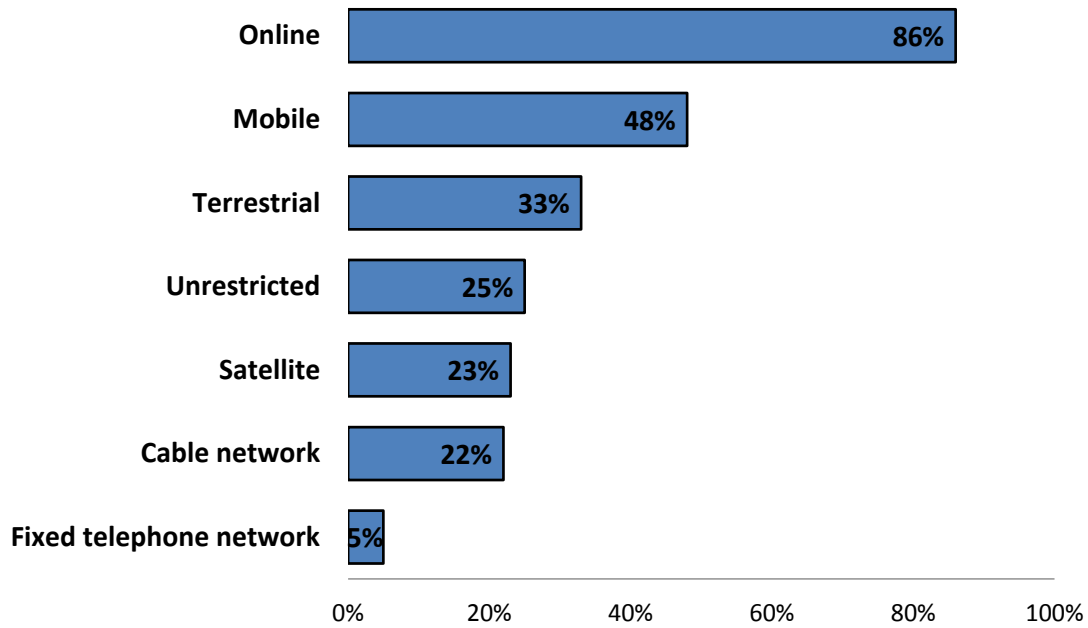
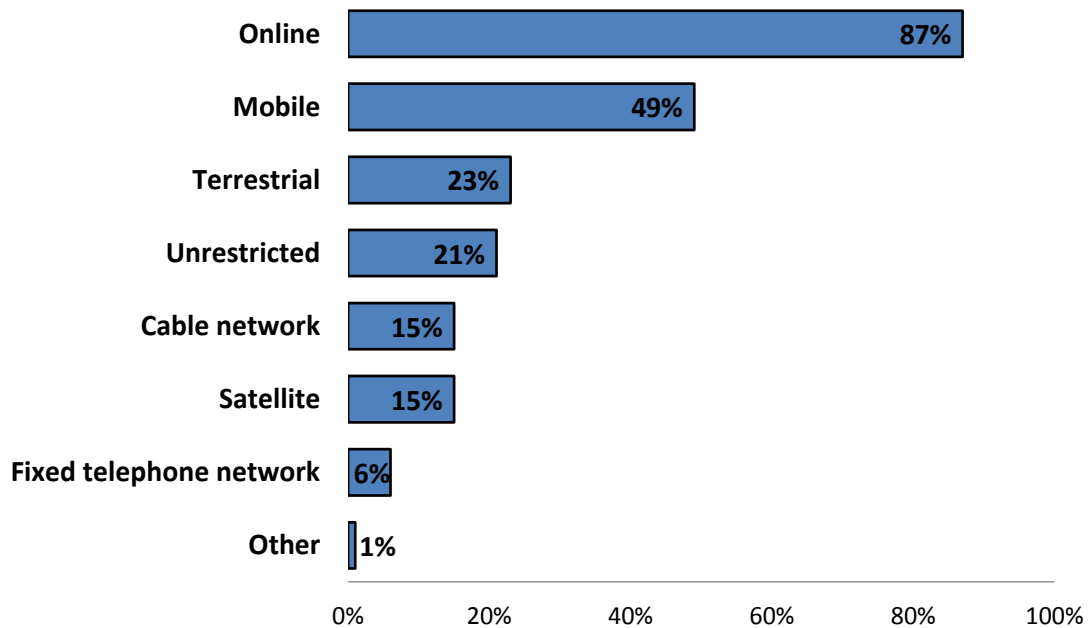


Figure C. 9: Proportion of agreements including specific transmission technology rights – Film agreements submitted by digital content providers



(651) Second, for news and non-television fiction, a sizeable minority of agreements include unrestricted rights as well as terrestrial rights. This is likely due to the fact that the majority of productions in these two product categories are from established national broadcasters, which often use terrestrial technology. The figures for these types of content are in Figure C. 10 to Figure C. 11.

Figure C. 10: Proportion of agreements including specific transmission technology rights – News agreements submitted by digital content providers

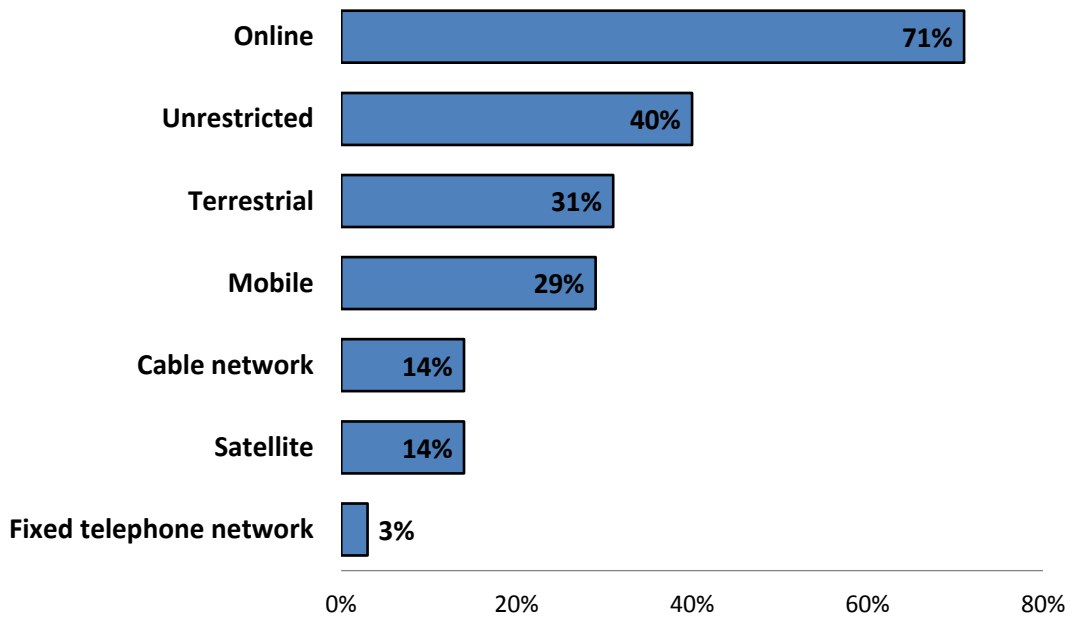
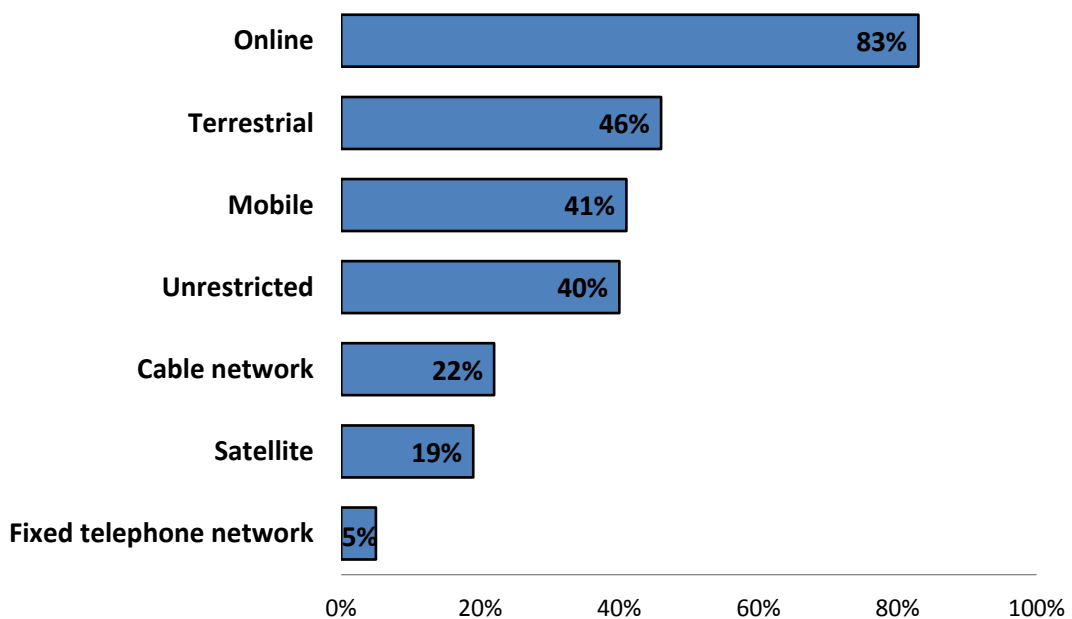


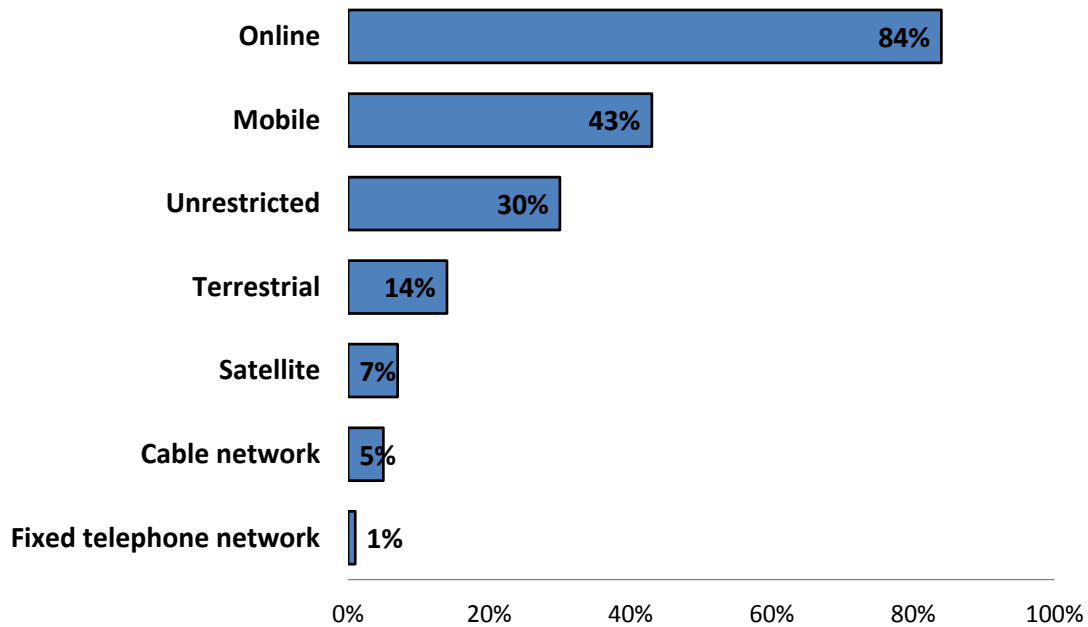
Figure C. 11: Proportion of agreements including specific transmission technology rights – Non-Television fiction agreements submitted by digital content providers



(652) Third, for music, most types of transmission technologies are not specified in the agreements. With the exception of online and mobile transmissions, all other types of transmission technologies are either rarely mentioned or implicitly licensed (as reflected by the "unrestricted" category).

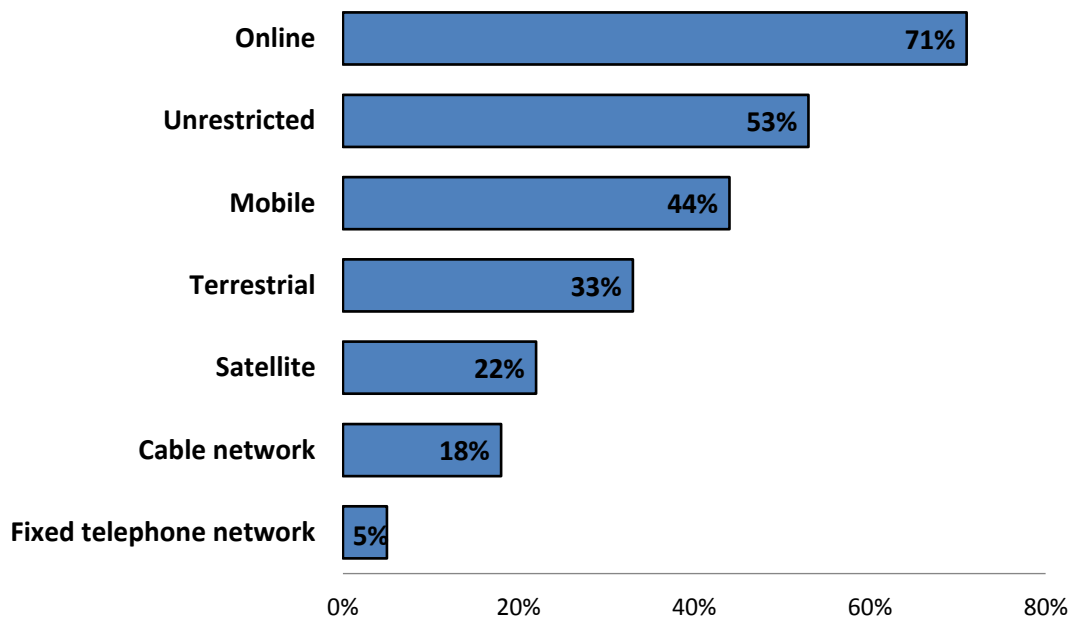
(653) This likely reflects the prevalence of online distribution for music products, which are now commonly consumed online or on mobile devices through streaming or transaction-based downloading models.

Figure C. 12: Proportion of agreements including specific transmission technology rights – Music agreements submitted by digital content providers



(654) Finally, for sports, the agreements are characterised by a higher proportion of unrestricted rights as well as a higher degree of specificity as regards licensed transmission technologies (Figure C. 13).

Figure C. 13: Proportion of agreements including specific transmission technology rights – Sports agreements submitted by digital content providers

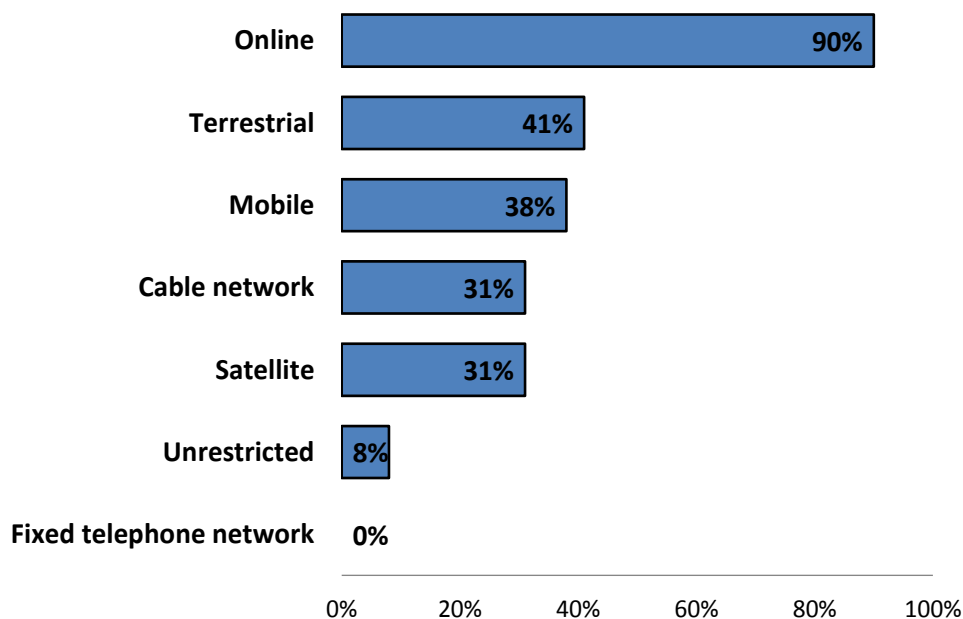


(655) Differences emerge also with regard to different types of operators.

(656) Public service broadcasters and commercial broadcasters tend to have a high proportion of agreements including rights relating to terrestrial transmission, mobile transmission, and a relatively high proportion of unrestricted transmission rights. For commercial broadcasters a sizeable proportion of agreements include rights on cable transmission as well.

(657) For mobile operators, (Figure C. 14) the proportion of agreements that contain unrestricted transmission rights is smaller.

Figure C. 14: Proportion of agreements submitted by digital content providers including specific transmission technology rights – Mobile operators



(658) The results of the sector inquiry indicate that online audiovisual operators have, on average, more detailed clauses in relation to transmission rights, as reflected by the relatively high proportion of agreements including at least one or more licensed transmission technologies. This category includes pay-TV providers as well as large online-only providers.

(659) At the other extreme, publishers and fixed network telecommunications operators (including both PSTN and cable operators) seem to typically conclude less specific agreements as regards transmission rights. This is likely due to the fact that most of these operators tend to be active in well-delineated geographic areas, which coincide with the size of their network.

(660) Finally, web TVs and portals have the greatest proportion of agreements including unrestricted transmission rights, with 67 % of agreements including such rights. This is in line with the fact that most of these operators produce their own content, which is then licensed within the same group or show user-generated content.

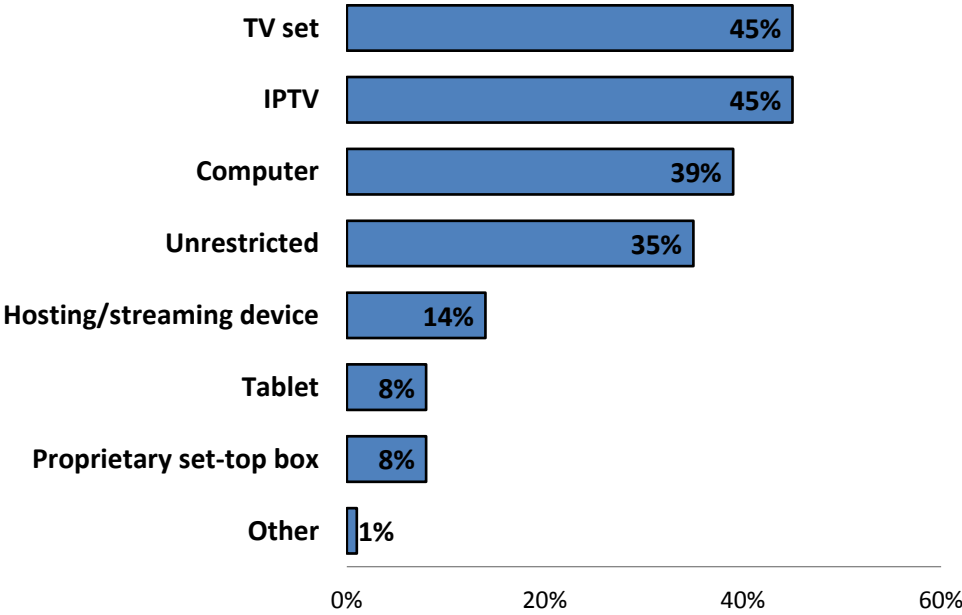
3.2. The scope of reception technology rights

(661) Contractual restrictions on reception technologies in agreements between right holders and digital content providers translate into restrictions on the types of services they can offer to users, and can be reflected in usage restrictions in agreements between digital content providers and users.

(662) In terms of reception technologies specifically or implicitly included in the licensing agreements of digital content providers, TV sets come on top when looking at the aggregated data (Figure C. 15), both in their traditional form as well as in the more recent "connected TV" variety. However computers of all types are also specifically mentioned in a substantial number of agreements (although still in the minority).

(663) Slightly more than a third of the agreements do not impose clear limits on the type of reception technology to be used by users of the services provided by digital content providers. However two thirds pre-define, and hence impose restrictions on, the type of device used to receive the transmission.

Figure C. 15: Proportion of agreements including specific reception technology rights – All agreements submitted by digital content providers

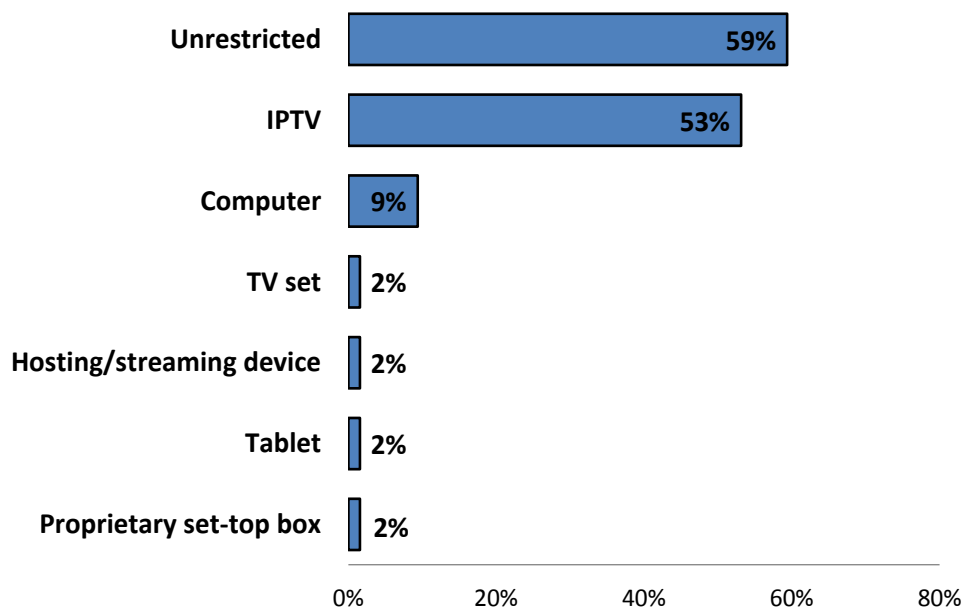


(664) The aggregate figures are representative of most types of content, with relatively significant variations only for films, music and news. In particular, film agreements are more specific about reception technologies. Music and news agreements are comparatively less specific. For these two latter types of agreements, it is comparatively more frequent that digital content providers allow users to receive content on any device.

(665) Finally, sports agreements include wider possibilities for digital content providers to allow users to receive content using any device, in line with the preliminary results in paragraph (654).

(666) In terms of reception technologies specifically or implicitly included in the agreements submitted by sports right holders (Figure C. 16), two results are noteworthy. First, connected TV sets are by far the most used reception technology with most other technologies being barely mentioned, except for computers. Second, unrestricted reception rights are used in the majority of agreements. This result is in line with what has been found in relation to digital content providers' sports agreements.

Figure C. 16: Proportion of agreements including specific reception technology rights – Sports right holders



(667) In terms of types of digital content providers, cable operators and online audiovisual providers have the most specific restrictions in terms of reception technologies in their agreements (Figure C. 17 and Figure C. 18 respectively).

Figure C. 17: Proportion of agreements submitted by digital content providers including specific reception technology rights – Cable operators

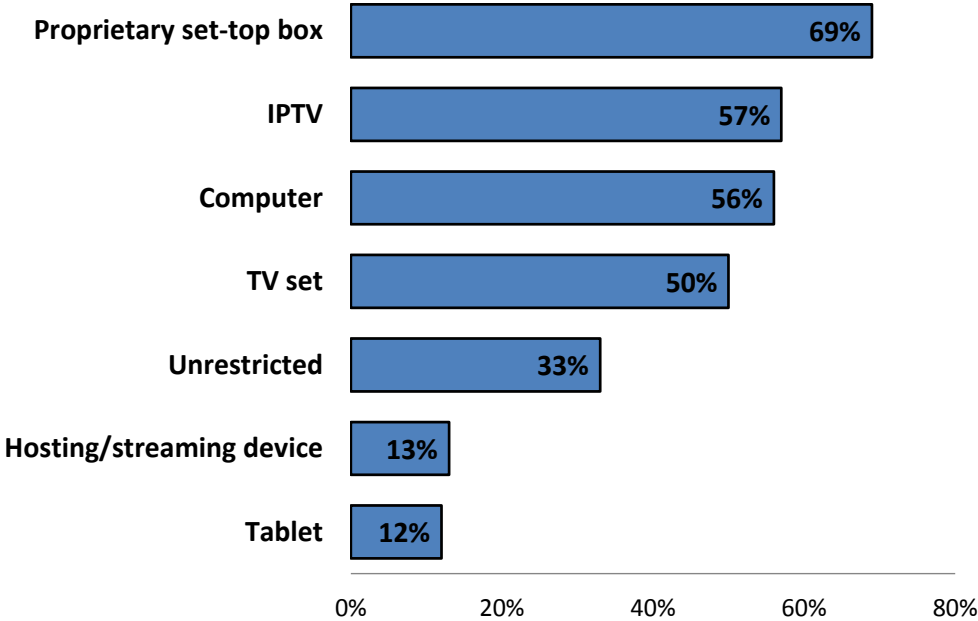
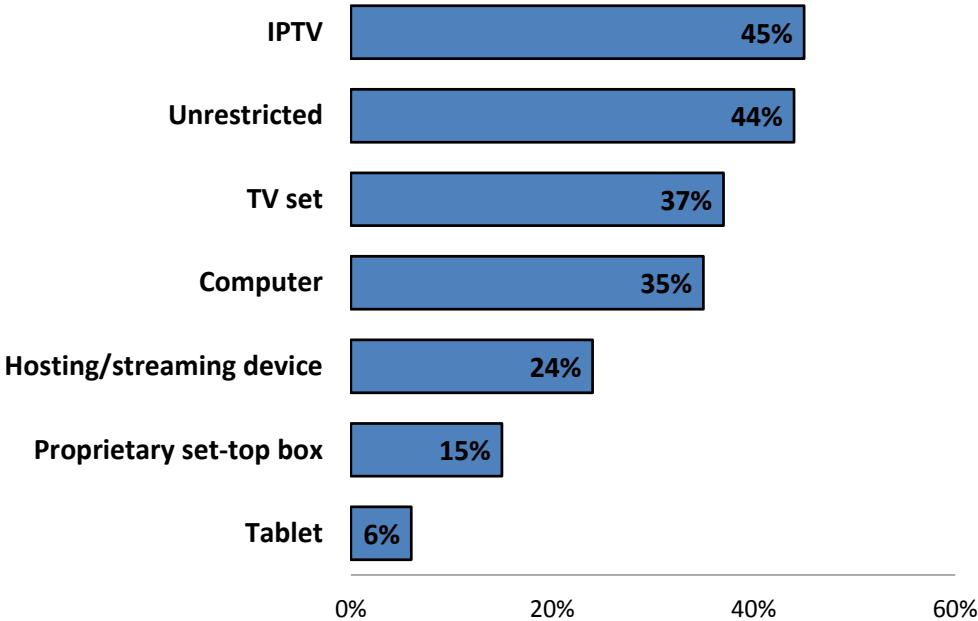


Figure C. 18: Proportion of agreements submitted by digital content providers including specific reception technology rights – Online audiovisual operators



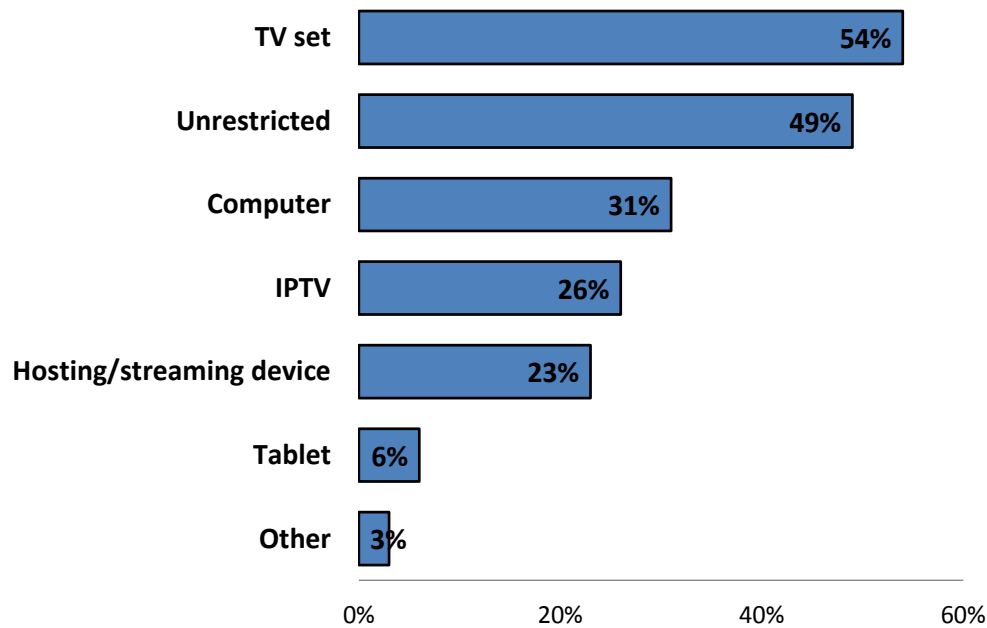
(668) In particular, most cable operators conclude agreements with right holders which limit the service to the use of set-top boxes, which almost always are designed to run on the specific cable operator's network. The agreements also define which devices can be used to access content after the set-top box has received and decoded the signal.

(669) Online audiovisual operators conclude agreements that allow the use any device in slightly less than half of the cases. This is probably due to the fact that many operators

in this category are seeking to provide a comprehensive, unrestricted service to users, who favour having the freedom to choose where and when to access content.

(670) Public service broadcasters (Figure C. 19) have the greatest proportion of agreements that do not specify which reception technologies can be used.

Figure C. 19: Proportion of agreements submitted by digital content providers including specific reception technology rights – Public service broadcasters



3.3 The scope of ancillary and usage rights

(671) Figure C. 20 provides an overview of the ancillary and usage rights (and of the corresponding technologies) for all agreements submitted by digital content providers.³³³ As can be seen from the figure, and again unsurprisingly given the focus of the sector inquiry on online distribution, providing content through streaming is mentioned in almost three quarters of agreements.

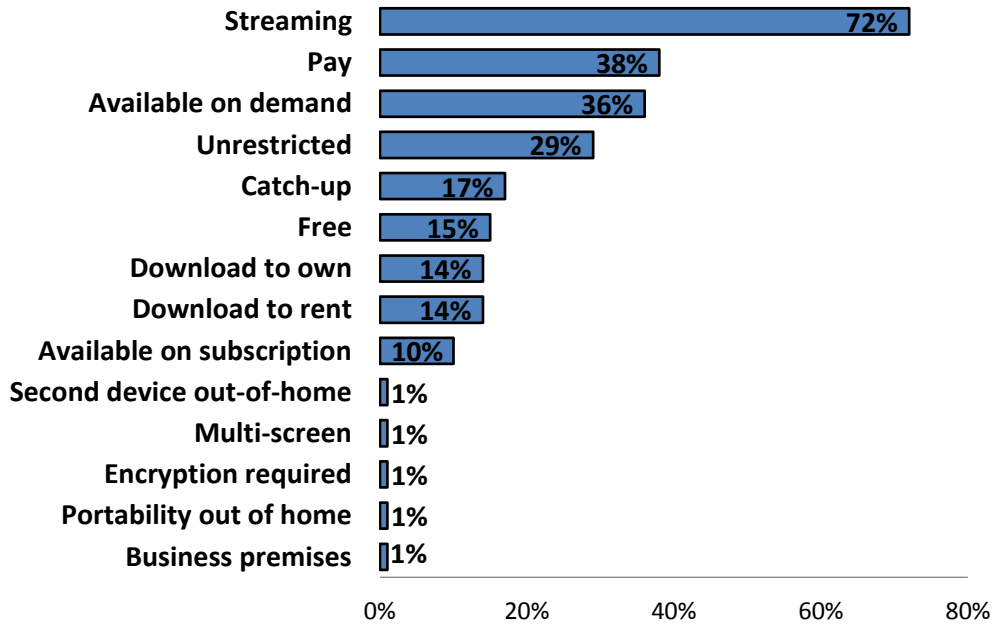
(672) Alternative distribution models for online content, such as "download to own" or "download to rent", are less frequent in the submitted agreements. This indicates that the streaming model is by now the prevalent one when it comes to accessing digital content online.

(673) Almost four out of ten agreements relate to paid services. This, in principle, means that digital content providers are contractually required to offer the relevant content through a paid service. By contrast, only 15 % of agreements relate to services that are free of charge. Less than one third of the agreements allow digital service providers to use the distribution model of their choice when allowing users to access the digital content they

³³³ As explained in footnote 330 many of the technologies listed can be combined.

offer. Figure C. 20 indicates that on demand is the most widely used business model with more than one third of all agreements including this possibility for digital content providers, compared to subscription models, which are mentioned in one out of ten agreements.

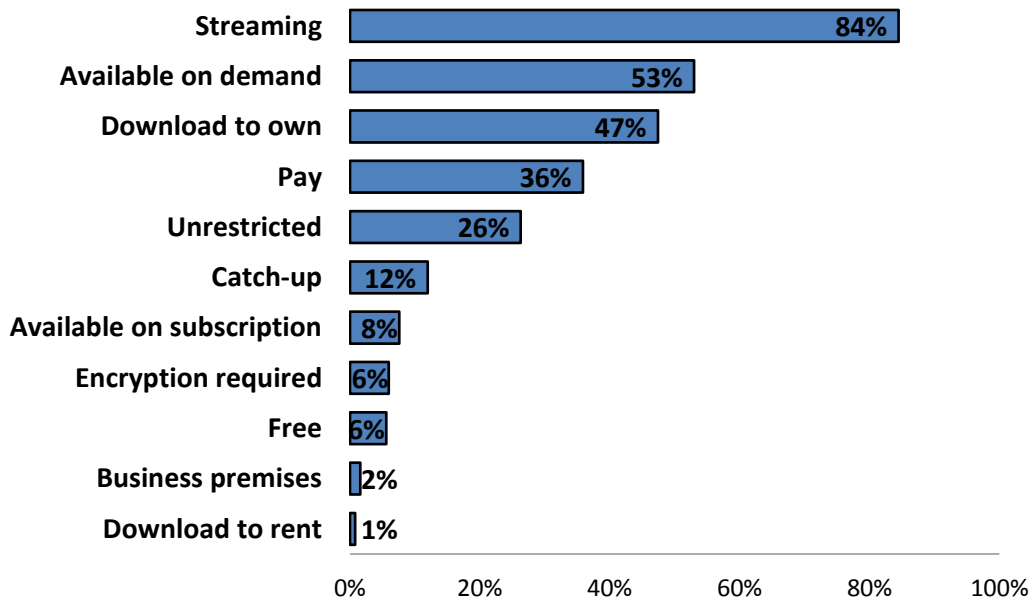
Figure C. 20: Proportion of agreements including specific ancillary and usage rights – All agreements submitted by digital content providers



(674) Similarly to what can be seen from the agreements submitted by digital content providers, the scope of licensing rights in the agreements submitted by right holders is defined precisely (Figure C. 21).

(675) In particular, on demand and download to own restrictions are frequently used and streaming remains by far the most used distribution model, even to a greater extent than seen in the agreements submitted by the digital content providers. More than a third of agreements specify that the buyer of rights has to offer paid services, and just over a quarter of agreements impose no restrictions on the business model of the digital content provider. Compared to digital content providers' agreements, a significantly lower proportion of agreements submitted by right holders specify that the service can be offered free of charge.

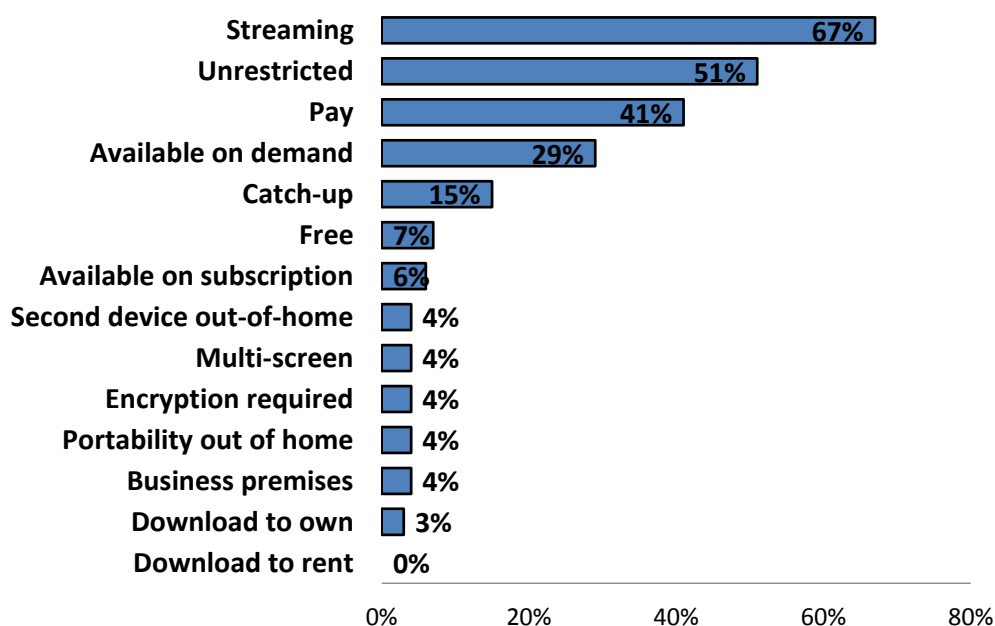
Figure C. 21: Proportion of agreements including specific ancillary and usage rights – All agreements submitted by right holders



(676) When looking at the different types of products, most restrictions are found in television fiction, film and sports agreements. In particular, both film and television fiction agreements include the possibility for operators to require payment and to operate an "on demand" model in relatively significant proportions. For both types of agreements, digital content providers are allowed to offer content for download to own and download to rent to a greater extent than the average.

(677) On the one hand, sports agreements are detailed in terms of the type of licensed ancillary rights (Figure C. 22). On the other hand, more than half of the agreements give content providers the freedom as regards the type of service they may offer, or how the content can be accessed by users.

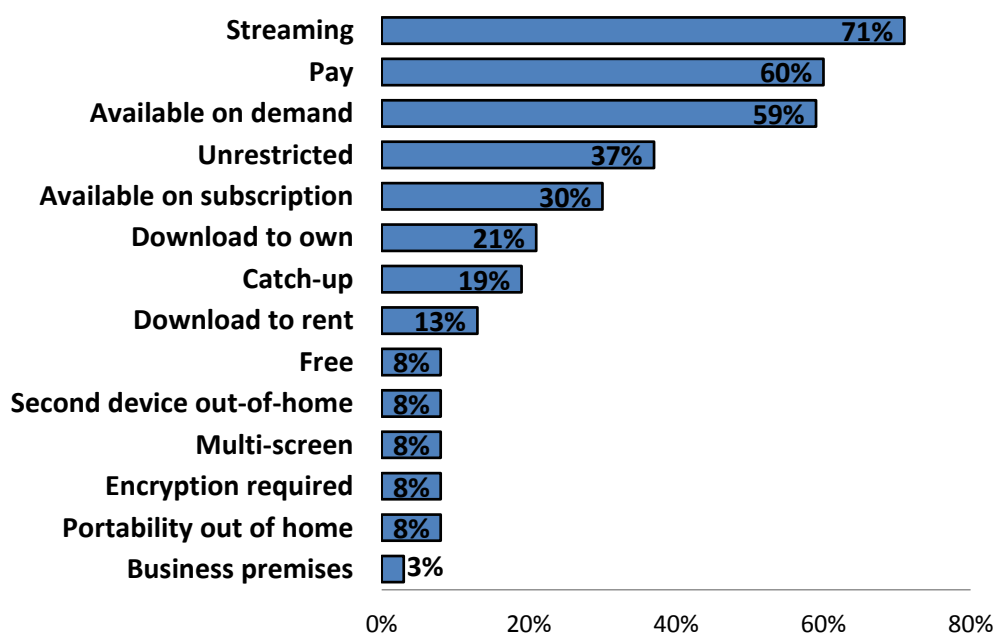
Figure C. 22: Proportion of agreements including specific ancillary and usage rights – Sports agreements submitted by digital content providers



(678) Licensing agreements of music right holders have a markedly lower level of specificity. Streaming is specifically mentioned in a majority of these agreements and paid services are specified in almost 30 % of agreements.

(679) Online audiovisual operators conclude licensing agreements containing the greatest number of restrictions with regard to ancillary and usage rights (Figure C. 23). Fixed line PSTN operators and mobile operators conclude agreements that include a lower number of usage restrictions.

Figure C. 23: Proportion of agreements submitted by digital content providers including specific ancillary and usage rights – Online audiovisual operators



(680) Publishers (i.e. print media businesses offering digital content, for example on their web sites) have one of the lowest proportions of restrictions related to paid services, as well as a relatively high proportion of restrictions relating to on demand and subscription content. This is consistent with the way print media web sites monetise their content, with a combination of subscription and advertising revenues.

3.4 Exclusive technology rights

(681) The licensing of technology rights is often coupled with exclusivity.³³⁴

(682) Right holders were asked to indicate which types of technologies were licensed exclusively, out of a list of pre-defined transmission and usage technologies. The figures below show the proportion of agreements submitted by right holders including exclusive rights for each of transmission (Figure C. 24) and usage (Figure C. 25) technologies.

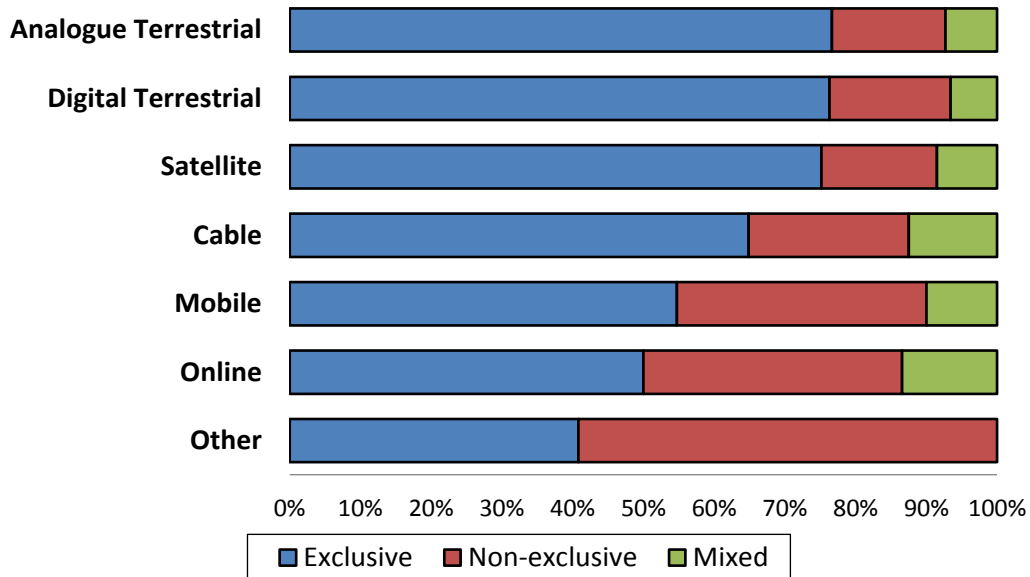
(683) Overall, the preliminary results confirm that technology rights are precisely defined in licensing agreements in order to license them exclusively.

(684) All of the technologies identified are licensed exclusively in at least half of the agreements submitted by right holders, except for the "other" category of transmission technologies. The use of exclusivity is likely to be more frequent than those proportions

³³⁴ As noted in section C.3.1, licensing of technology rights means licensing of the rights to economically exploit certain content through the use of a specific technology.

suggest, as "mixed" exclusivities are often almost equivalent to full exclusivities, with a few exceptions.³³⁵

Figure C. 24: Proportion of agreements including exclusive transmission technology rights – All agreements submitted by right holders



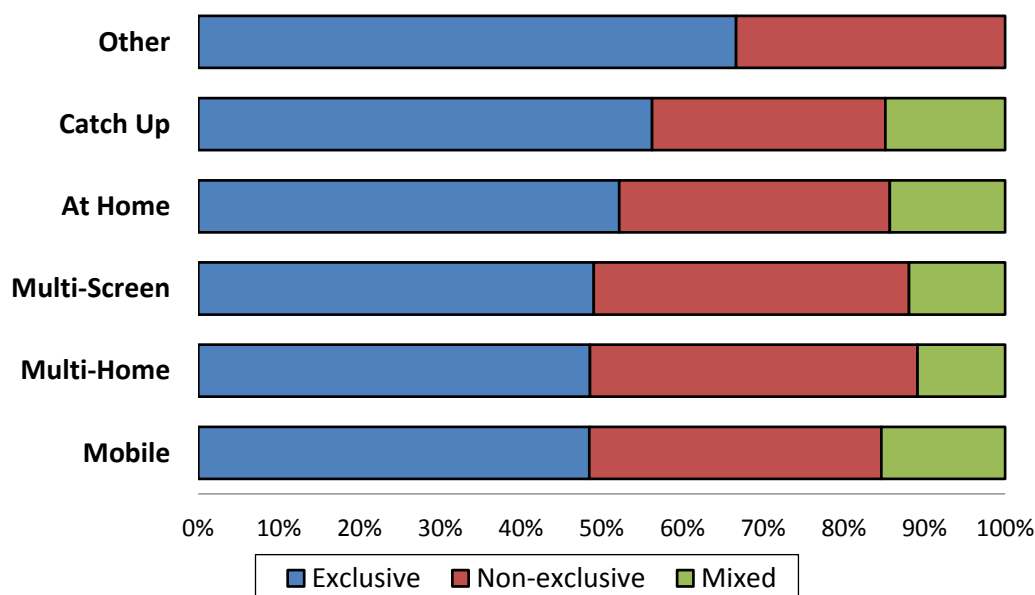
(685) In terms of transmission technologies, exclusive licensing is mainly used for terrestrial and satellite rights, and, to a slightly lesser extent, for cable and mobile rights.

(686) Online rights are less often licensed on an exclusive basis, with about half of the agreements including exclusive online transmission rights. Online transmission also has the highest proportion of agreements including non-exclusive rights, together with mobile transmission (and excluding other technologies).

(687) In terms of ancillary / usage rights more than half of agreements are exclusive. A large part of the "other" category includes unrestricted rights or other types of rights, such as the right to offer the content to business users. However there were relatively few respondents selecting the "other" category, hence the importance of this result should not be overestimated.

³³⁵ A large number of right holders respondents failed to indicate in what sense the exclusivity was "mixed." Those who did so often indicated that exclusivity was limited only in relation to certain release windows, for example when the products are delivered through VOD or SVOD services.

Figure C. 25: Proportion of agreements including exclusive ancillary and usage technology rights – All agreements submitted by right holders



(688) The preliminary results set out in Figure C. 25 confirm that exclusivity is widely used in relation to transmission and usage technologies.

3.5 Bundling of rights

(689) The preliminary results of the sector inquiry show that rights for online transmission of content are to a large extent licensed together with the rights for other transmission technologies (such as satellite, cable or mobile).

(690) Respondents have indicated that rights for online transmission are often included as part of a package of licensed rights regardless of whether the contracting party is actually active in online distribution of digital content or not.

(691) Consequently, most respondents were not able to provide a separate value of the online rights covered by a licensing agreement. Several of them have indicated that the value of online rights is minimal in comparison to other rights covered by the licensing agreements.

3.5.1 Prevalence of bundling of rights

(692) Figure C. 26 and Figure C. 27, below, show that in 79 % of the licensing agreements submitted by digital content providers and in 89 % of the agreements submitted by right holders, online rights are licensed together with rights in other transmission technologies.

Figure C. 26: Proportion of licensing agreements that contain only online rights respectively online rights together with rights in other transmission technologies – All agreements submitted by digital content providers

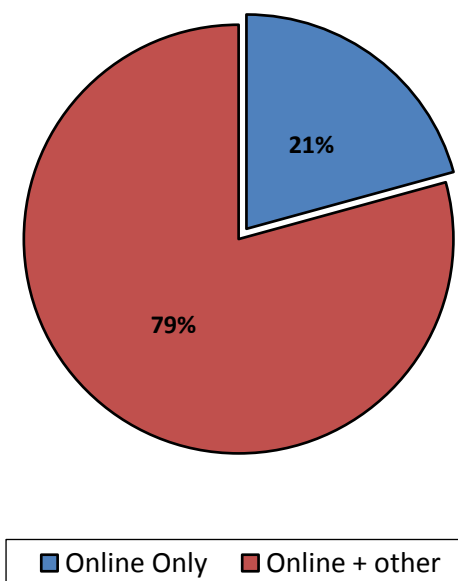
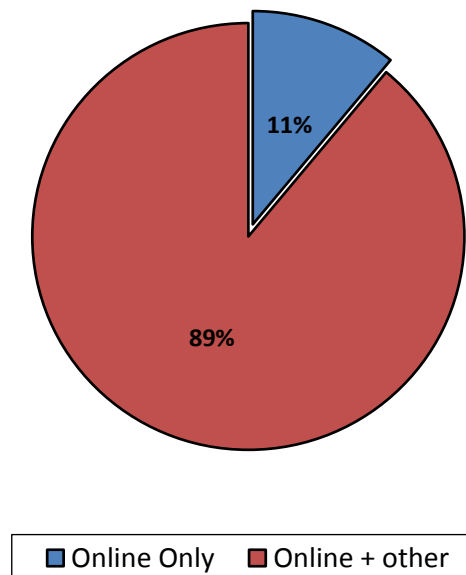
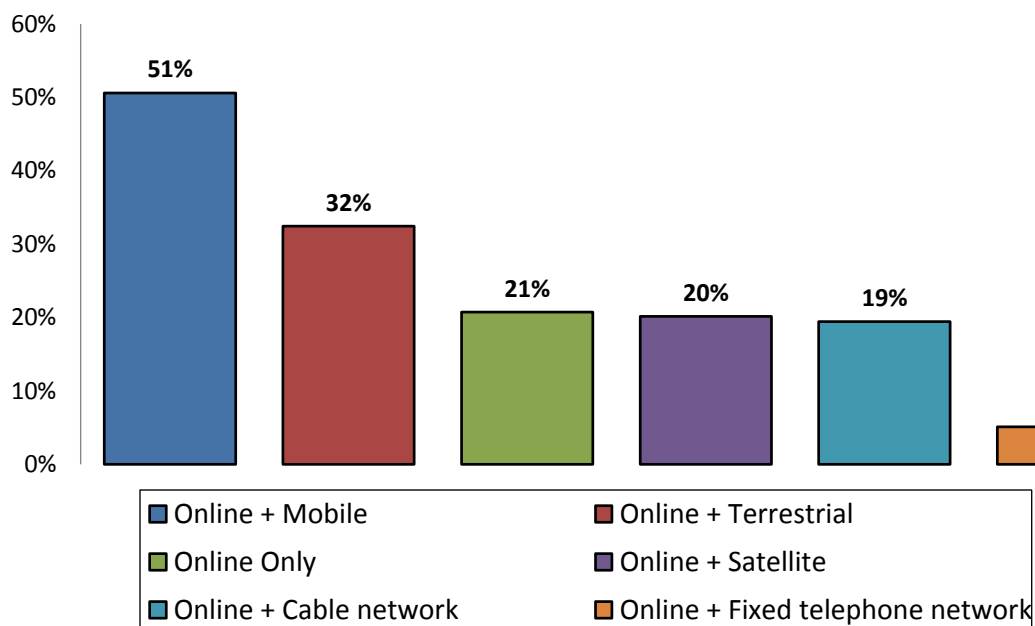


Figure C. 27: Proportion of licensing agreements that contain only online rights respectively online rights together with rights in other transmission technologies – All agreements submitted by right holders



(693) According to the preliminary results presented in Figure C. 28 below, online rights are most often licensed together with rights for mobile transmission, terrestrial transmission and satellite transmission.

Figure C. 28: - Proportion of agreements containing different combinations of online rights with rights in transmission technologies other than online – All agreements submitted by digital content providers



3.5.2 Bundling of rights

(694) Bundling rights for online transmission with rights in other transmission technologies may limit the availability of a varied offer of digital content services to users and may lead to a restriction of output, in particular where the online rights are not, or only partly, exploited by the licensee. Bundling of rights may also hinder both existing operators and new entrants from competing and developing new innovative services, which in turn may reduce consumer choice.

Summary

The precisely defined scope of technology rights licensed to digital content providers has wide-ranging implications for their operations, including their business model, the service they can provide, and the reception infrastructure they can use. The practice of splitting rights according to technologies, including the modalities for offering / accessing the service, means that a complex patchwork of licensed rights is often created in the same Member State, the structure of which is highly dependent on existing commercial relationships between right holders and digital content providers. The widespread use of exclusivity in conjunction with the licensing of technology rights implies that both new entrants and existing operators which do not have access to specific technology rights might find it difficult to acquire online transmission rights, depending on how such rights have been licensed (split up) and to which company in a particular territory.

Moreover, rights for online transmission of digital content are to a large extent licensed together with the rights for other transmission technologies. Agreements submitted by digital content providers indicate that online rights are the most often licensed together with rights for mobile transmission, terrestrial transmission and satellite transmission. Bundling of rights

may not only negatively impact users in the sense of reducing the availability of content, but may also prevent other operators from competing specifically for online services.

4. THE SCOPE OF LICENSED RIGHTS: TERRITORIES

4.1 Introduction

(695) The preliminary results of the sector inquiry show that online rights are to a large extent licensed on a national basis. Online rights are often licensed bundled with rights for the distribution of content via other transmission technologies. The territorial scope of online and offline rights is therefore often the same, as offline rights are traditionally licensed on a national basis.

(696) Moreover, right holders have indicated in their responses that their business models are built on licensing of rights on a national basis. This allows them to extract the highest possible value from the rights in terms of revenues.

4.2 The territorial scope of online rights

(697) The fact that online rights are in the large majority of cases licensed on a national basis is confirmed by the replies and the licensing agreements submitted by digital content providers. According to Figure C. 29 below, 57 % of the online rights licensed under all the licensing agreements submitted by content providers, and independently of the content category, type of operator and type of business model, were licenced for the territory of one Member State only.

(698) Figure C. 29 also shows that online rights are to a non-negligible extent (21 %) obtained for territories covering between two and four Member States. Digital content providers that are distributing content using other transmission technologies than online transmission and that have decided to expand their commercial activities beyond the territory of one Member State only, have often chosen to enter neighbouring countries with the same or similar language. This is also true for online rights when those are licensed for a territory covering more than one Member State. The preliminary results of the sector inquiry show that the Member States which are often grouped together and for which both online and other rights are often licenced together, are (i) the territories of France and the French speaking parts of Belgium and Luxembourg, (ii) the UK and Ireland, (iii) Germany and Austria, (iv) the Benelux countries, (v) the Nordic countries, and (vi) the Czech Republic and Slovakia.

(699) The replies and licensing agreements submitted by rights holders confirm the conclusions drawn from the analysis of the replies and licensing agreements submitted by digital content providers that online rights are mainly licensed nationally or for a territory covering between two and four Member States. As Figure C. 30 below shows, an almost equal number of the licensing agreements submitted by right holders cover the territories of either one Member State (35 %) or two to four Member States (40 %).

(700) Online rights are to a lesser extent licensed on a pan-EU level. The replies from both digital content providers and right holders show that this is in particular true for the categories of content that may contain premium content products, such as sports, films and fiction TV (see Figure C. 29 and Figure C. 30 below). According to Figure C. 29, 15 % of all examined agreements submitted by digital content providers cover the territories of all the 28 Member States. The number is almost the same, 13 %, for the agreements submitted by right holders (Figure C. 30). Figure C. 31 and Figure C. 32 below indicate that the extent to which rights are licensed on a pan-EU basis varies between different content categories.

Figure C. 29: Proportion of agreements including rights licensed for a certain territorial scope – All agreements submitted by digital content providers

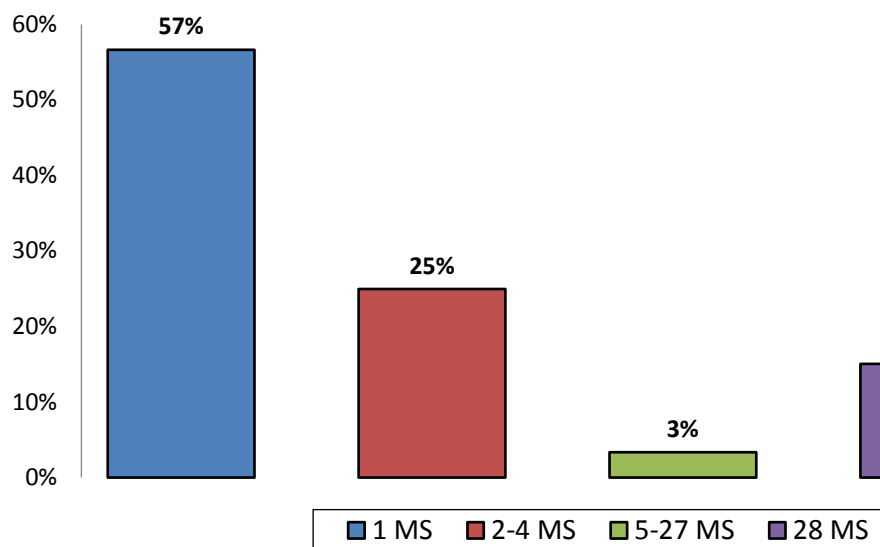
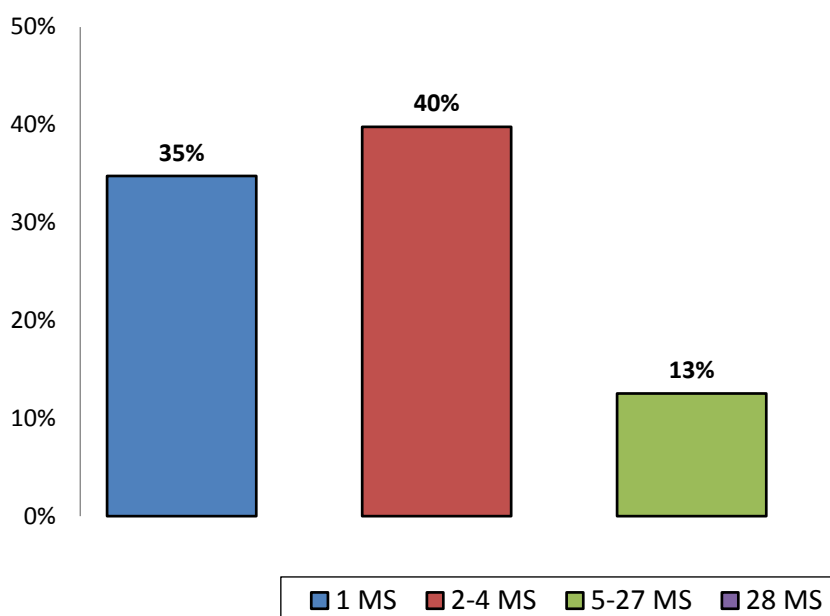


Figure C. 30: Proportion of agreements including rights licensed for a certain territorial scope – All agreements submitted by right holders



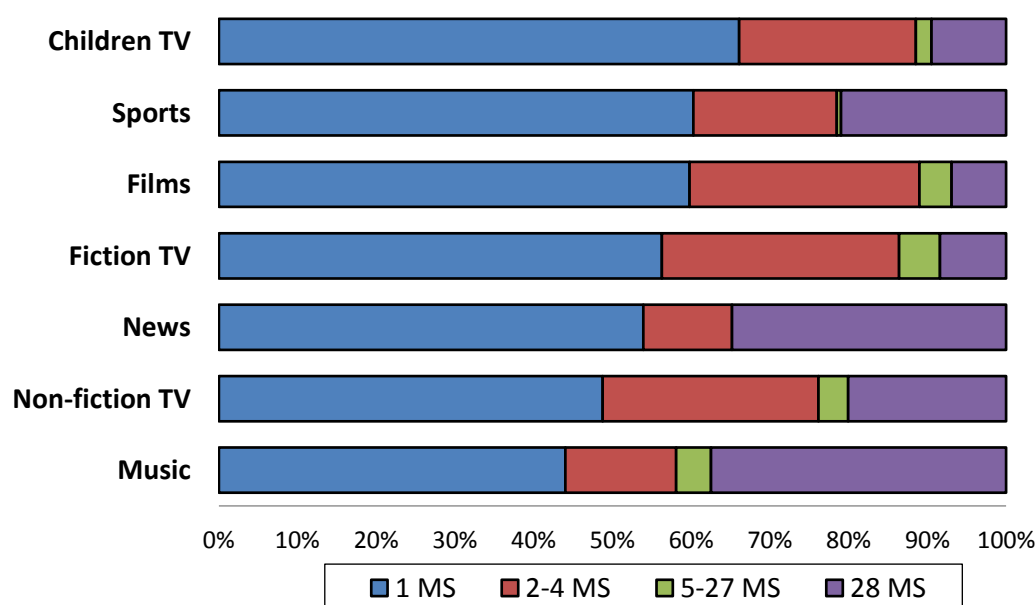
4.2.1 The territorial scope of online rights in relation to different types of digital content

(701) Figure C. 31 below indicates that in relation to all the defined content types, 45 % or more of the rights covered by the licensing agreements submitted by digital content providers are licensed for the territory of one Member State only. This confirms the prevalence of territorial licensing (i.e. licensing on a per Member State basis). Licensing of rights on a national basis is particularly prevalent in relation to content types that may contain premium products, such as children TV (66 %), sports (60 %), films (60 %) and fiction TV (56 %).

(702) According to Figure C. 31, music and news are the content categories for which rights are most often licensed on a pan-EU basis (38 respectively 35 %), followed by sports (21 %) and non-fiction TV (20 %). This may be the result of the scope of the commercial activities of certain digital content providers in these sectors. Another relevant factor is the interest in and consumer demand for specific content, based on cultural and linguistic differences.

(703) The fact that both news and sports at the same time to a rather large extent are licensed on a national basis (54 respectively 60 %), may be explained by the fact that news and sports broadcasts are often both produced and distributed by content providers, that operate on national basis (such as public service broadcasters). Furthermore, some of this type of content is of only national interest.

Figure C. 31: Proportion of agreements including rights licensed for a certain territorial scope – All agreements submitted by digital content providers – By product type



(704) The licensing agreements submitted by right holders show differences in the territorial scope of rights depending on the type of content that is covered by the agreements. As follows from Figure C. 32 below, while 67 % of the rights licensed by music right holders cover 28 Member States and only 22 % cover one Member State, the

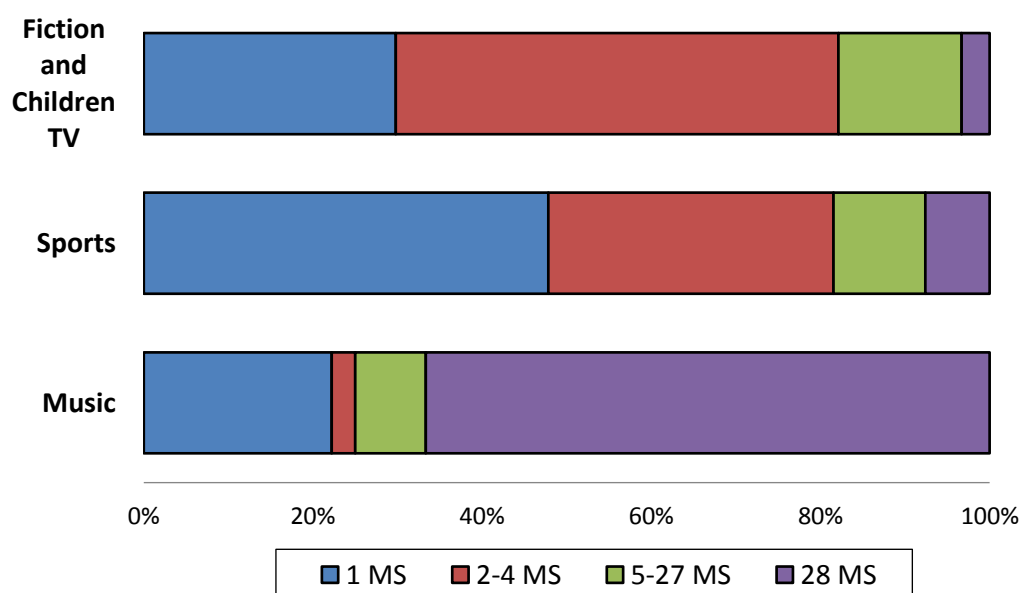
preliminary results are rather different in relation to right holders that license sports and/or fiction and children TV content.

(705) A majority of the licensing agreements submitted by sports rights holders (48 %) covers the territory of one Member State only, and only a minor part of such agreements (8 %) provide licenses on a pan-EU basis. These figures confirm the preliminary results of the analysis of the licensing agreements submitted by digital content providers, in the sense that rights in sports are most often licensed on a national basis. As explained above, the two sets of results can however not be compared in absolute terms since the two data sets are different. In the agreements submitted by digital content providers, there is also a rather high percentage (34 %) of rights licensed for a territory covering between two and four Member States.

(706) Figure C. 32 moreover shows that the territorial scope of around 30 % of the licensing agreements submitted by fiction and children TV rights holders cover the territory of one Member State only and only 3 % of the agreements have a pan-EU scope.

(707) Around half of the licensing agreements (52 %) of fiction and children TV rights holders that were examined in the course of the sector inquiry cover a territory of between two and four Member States. This corresponds largely to the replies submitted by digital content providers, as follows from Figure C. 31 above.

Figure C. 32: Proportion of agreements including rights licensed for a certain territorial scope – All agreements submitted by right holders - By product type



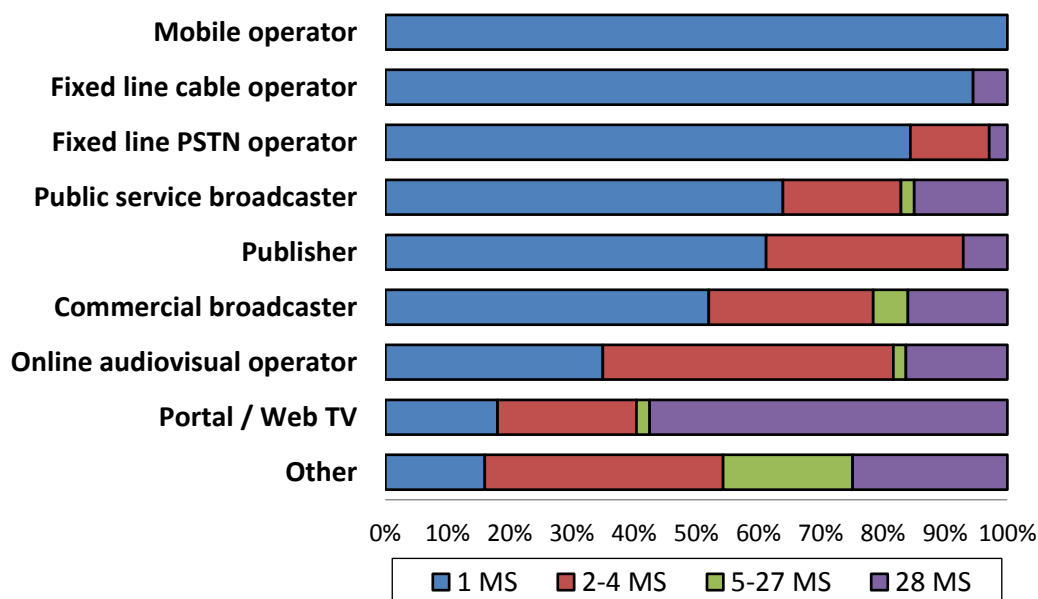
4.2.2 The territorial scope of online rights in relation to different types of digital content providers

(708) Figure C. 33 below shows the territorial scope of the licensing agreements submitted by digital content providers in relation to the different identified types such operators. Agreements which exclusively or to a large extent cover the territory of only one

Member State between right holders and each type of operator are agreements between mobile operators (100 %) fixed line cable operators (94 %) and fixed line PSTN operators (84 %). This can be explained by the fact that the business models of these operators as well as the infrastructures used by them for the distribution of content are generally national in scope.

- (709) Public service broadcasters, which traditionally operate on a national basis, to a large extent obtain the rights in digital content on a per Member State basis. 64 % of the agreements submitted by public service broadcasters cover the territory of one Member State only.
- (710) Commercial broadcasters mainly obtain online rights on a national basis (52 %) and to some extent also for the territories of two to four Member States (26 %). This may be explained by the differences in size and type of the activities pursued by the commercial broadcasters that responded to the sector inquiry. Some of these operators offer their content services on a regional basis. The fact that a non-negligible number of rights (16 %) were obtained on a pan-EU basis may relate to the specific content covered. It seems from the preliminary results that "older" or "non-premium" content, in relation to which there may not be an interest in licensing on an exclusive, national basis at a premium price, may be offered on a pan-EU basis.
- (711) The operators that obtain the most online rights on a pan-EU level (58 %) are the portal/web TV operators that only have online activities.
- (712) Online audiovisual operators predominantly obtain online rights on a regional level, for the territories of two to four Member States (47 %), but also to a rather large extent for the territory of one Member State (35 %). A smaller percentage of the agreements (16 %) including rights that are licensed to online audiovisual operators have a pan-EU scope. This variety in territorial scope of the licensing agreements, may be explained by the fact that this is a heterogeneous group of operators which includes both operators that mainly pursue their commercial activities in one Member State only (e.g. because they have traditionally been distributing content on a national basis via other transmission technologies than online, such as operators offering paid services), as well as operators whose activities are EU-wide in scope (such as pure online operators).

Figure C. 33: Proportion of agreements including rights licensed for a certain territorial scope – All agreements submitted by digital content providers- By type of operator



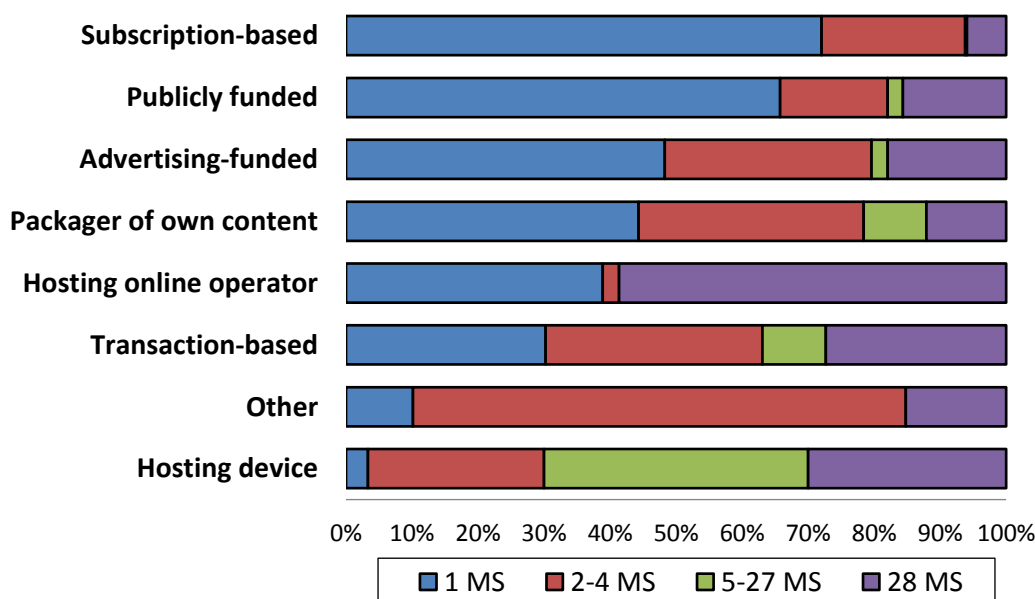
4.2.3 The territorial scope of online rights in relation to the different business models used by digital content providers

(713) Figure C. 34 below shows the territorial scope of the submitted licensing agreements by type of business model used by the different digital content providers. The responses and licensing agreements submitted by hosting online operators show that online rights are to a large extent licensed to them on a national basis, despite the fact that the services provided by these operators often can be accessed and used by users in most of the Member States.

(714) Online rights are licensed mainly on a national basis also to content providers operating on the basis of a subscription-based business model (72 %), such as mobile operators, fixed line cable operators and fixed line PSTN operators. Figure C. 34 thus confirms to a large extent the preliminary results shown in Figure C. 33 above in relation to these types of operators, i.e. that they mainly obtain rights on a national basis. Packagers of own content is another category of distributors that mainly obtain rights on a per Member State basis. These results suggest that rights holders typically tend to license rights on a national basis.

(715) The business model "hosting online operator" is by far the category in relation to which most of the online rights are licensed on a pan-EU basis (59 %). This category is followed by hosting devices (30 %) and transaction-based business models (27 %). The latter business model includes distributors whose commercial activities are specifically tailored to online distribution, such as so-called Over The Top (OTT) operators. These operators are often online-centric and can deliver their services via media streamers, hosting devices, videogame consoles and increasingly often directly to hosting-capable connected TV sets.

Figure C. 34: Proportion of agreements including rights licensed for a certain territorial scope – All agreements submitted by digital content providers - By type of business model



4.3 Exclusive territorial rights

(716) As for technology rights, exclusivity is often also used in association with a territorial scope of the licensing agreement.

(717) Right holders were asked to indicate for each of the covered territories, whether the rights were licensed on an exclusive or non-exclusive basis.

(718) In the analysis that follows, rights can be exclusive, non-exclusive, or mixed. The "mixed" category covers instances in which the exclusivity may not apply to all territories, e.g. right holders may have granted exclusive rights to digital content providers only for certain of the Member States covered by an agreement but not in all of them.

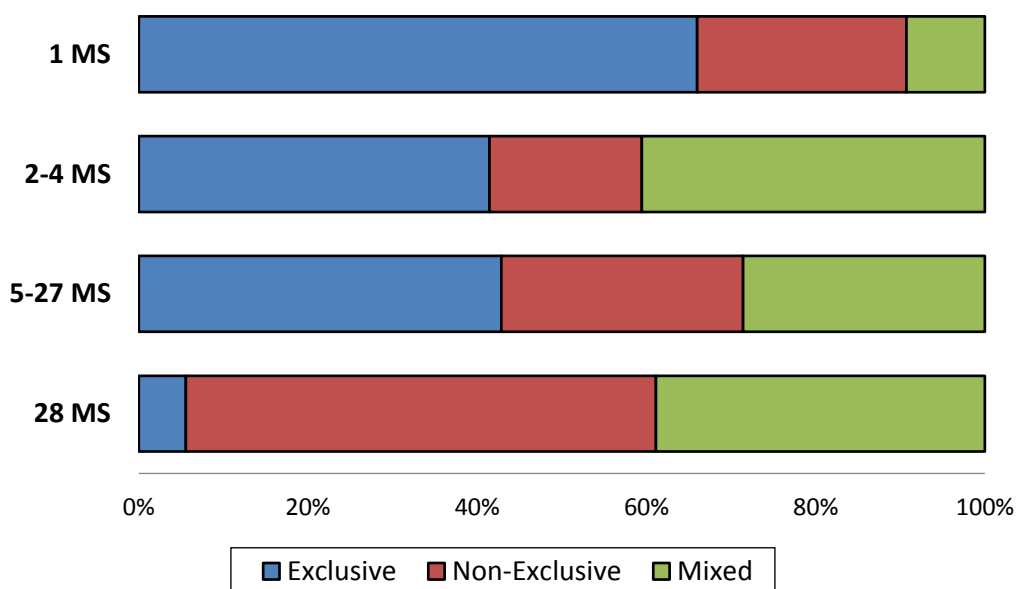
(719) Conversely, the "exclusive" category refers to instances in which the right has been conferred in full to a digital content provider that has also been granted exclusivity, for all territories. The "mixed" and "exclusive" categories thus provide an idea at the extent to which territorial exclusivity is used, as can be seen in Figure C. 35 below.

(720) Figure C. 35 below shows that rights are most often exclusive when they are licensed for the territory of one Member State only. In those cases, 66 % of the submitted agreements were licensed on an exclusive basis.³³⁶

³³⁶ It may seem contradictory that 12 % of the agreements that concern one Member State only include "mixed" rights. The replies show that these most often relate to the situation where an agreement covers one Member State, as well as other non-Member States and that the rights are licensed exclusively for some of the territories covered by the agreement but not for all.

(721) At the same time, Figure C. 35 shows that non-exclusive rights tend to be licensed on a pan-EU basis.

Figure C. 35: Proportion of agreements including exclusive / non-exclusive rights licensed for a certain territorial scope – All agreements submitted by right holders



4.4 Reasons for non-availability of content across borders

(722) Online rights are in the large majority of cases licensed on a national basis or for the territory of a few Member States only. On the basis of all licensing agreements submitted by digital content providers, and independently of content category, type of operator and type of business model, 57 % of the online rights licensed on the basis of these agreements cover the territory of one Member State only. The content licensed through those agreements is thus not available to users in other Member States who seek to access it through that specific digital service provider.³³⁷

(723) In order to understand why some providers of digital content services make their services accessible to users that are located only in one Member State or in a limited number of Member States, respondents that replied that their services were not available in certain Member States were asked to provide the reasons for their reply.

(724) They were asked to rate eleven different reasons³³⁸ on a scale between 1 and 5, where 1 indicates that the reason has no influence at all and 5 that the reason is decisive for their

³³⁷ The same content could of course be available to users in other Member States through other providers.

³³⁸ The reasons given in the questionnaire were the following: cost of obtaining information about consumer protection laws; costs of complying with consumer protection laws; other compliance costs (e.g. tax laws); cost of purchasing content for those territories; content is not available to purchase in those territories; appropriate language versions are not available for those territories; cost of preparing appropriate language versions for those territories; user interface translation costs; costs of adapting business model to obtain revenue from users in those territories (e.g. by seeking advertisers in those territories); inadequate infrastructure (e.g. broadband speed) in those territories and insufficient consumer demand.

choice not to enter certain national markets. In their reply, respondents could indicate more than one reason as having no influence at all respectively as being decisive for the decision to provide digital content services in a specific Member State.

(725) The respondents were also given the option to indicate if there were other reasons than the ones given that were relevant for their decision to make content available or not in other Member States. Some respondents provided explanations for their replies, of which examples are given below. Table C. 6 shows the proportion of respondents that considered the given factors to be of highest importance (i.e. they rated the factor with a 4 or a 5 on a scale of 1 to 5) when being asked to rank the reasons why they do not make their content services accessible in some Member States.

Table C. 6: The most important factors for a digital content provider not to make its services accessible in Member States other than those in which it currently operates

Other	68.9%
Cost of purchasing content for those territories	67.1%
Content is not available to purchase in those territories	54.3%
Costs of adapting business model to obtain revenue from users in those territories	46.6%
Insufficient consumer demand	39.7%
Cost of preparing appropriate language versions for those territories	35.6%
Appropriate language versions are not available for those territories	31.1%
User interface translation costs	20.3%
Other compliance costs (eg tax laws)	13.9%
Inadequate infrastructure (eg broadband speeds) in those territories	13.0%
Costs of complying with consumer protection laws	10.1%
Costs of obtaining information about consumer protection laws	2.8%

(726) The highest proportion of respondents indicated that there are "other" reasons than those listed in the questionnaire for digital content providers not to make their services accessible in other Member States. However, the replies show that some of the respondents failed to explain what these other reasons are or that they actually indicated one of the given reasons in their reply under the option "other" reasons, such as that the content is not accessible for purchase in some territories. Other respondents provided reasons linked to the specific business choices of the company in question, such as the size of the business and the focus of the business model on specific territories. A few respondents invoked the competitive landscape as a reason for not making their services accessible in certain Member States, as well as costs for marketing and advertising.

- (727) Besides the "other" category, a majority of the content providers indicated that the most important reason for not making content accessible in other Member States, out of the eleven reasons that were given in the questionnaire, is the cost of purchasing content for territories in which the digital content provider is not yet active. In particular, smaller operators or operators in smaller Member States indicate that they have limited their activities to one or a few Member States, since it would be too expensive to acquire the rights for other territories. Therefore, they can only make their services available in a limited number of Member States and are thus prevented from offering subscribers the possibility to access and use their services from other Member States.
- (728) The second most important of the given reasons (besides the "other" category) for not making content accessible in other Member States was that the rights in the content are not available for licensing for (some or all) of the territories of those Member States. In this respect, respondents state that some right holders make the licensing of their content conditional upon the fact that the digital content provider undertakes to apply geo-blocking, or that they would need to pay higher fees in order to make some content available without geo-blocking. Respondents also explain that the business models of some right holders do not allow the digital content providers to offer portability of their services. Some respondents moreover indicate that the rights in certain content are limited to specific language versions, which are only interesting for consumers in certain Member States.³³⁹
- (729) Some content providers moreover indicate that they would be interested in extending the reach of their digital content services, also by providing cross-border services, but that they encounter difficulties in acquiring the necessary rights.
- (730) Table C. 7 below shows which of the given factors were considered by the respondents to be of least importance (i.e., the respondents rated the factor with 1 or 2 on a scale of 1 to 5) when being asked to explain why they do not provide content services in some Member States.

³³⁹ The categories "cost of purchasing content" and "content is not available for purchase" are somewhat related but look at different things. High costs of purchasing certain content can dissuade a potential buyer from entering into a licensing agreement with the holder of the rights to that content even when those rights are available for purchase.

Table C. 7: The least important factors for a digital content provider not to make its services accessible in Member States other than those in which it currently operates

Costs of obtaining information about consumer protection laws	81.7%
Other compliance costs (eg tax laws)	80.6%
Costs of complying with consumer protection laws	78.3%
Inadequate infrastructure (eg broadband speeds) in those territories	69.6%
User interface translation costs	59.4%
Appropriate language versions are not available for those territories	56.8%
Cost of preparing appropriate language versions for those territories	50.7%
Insufficient consumer demand	43.8%
Costs of adapting business model to obtain revenue from users in those territories	34.2%
Content is not available to purchase in those territories	30.9%
Other (please specify)	24.6%
Cost of purchasing content for those territories	20.0%

(731) As indicated in the table above, the costs for obtaining information in order to comply with the law, such as tax laws, as well as the costs for complying with consumer protection laws are the least important reasons for not making content services available in certain Member States. Other content providers also consider that infrastructure-related issues, such as the fact that the infrastructure in certain Member States is inadequate for example in terms of broadband speed, are not relevant for their choice to make their services accessible or not by users in those Member States.

4.5 Catalogue differences

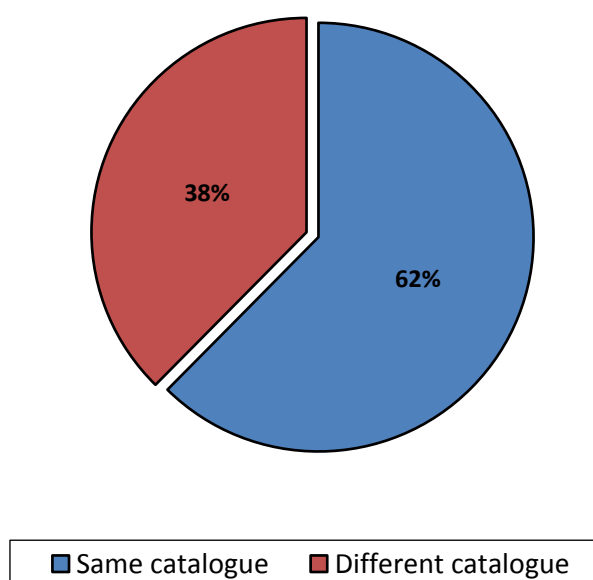
(732) Digital content providers that make their services available in two or more Member States do not necessarily offer the same catalogue of content to users in each of those Member States. On the contrary, it is rather common that the content available to users in one Member State differs from that available to users in other Member States.

(733) In this respect, respondents were asked whether there are any differences in the catalogue of content that they offer to users in different Member States.

(734) Of the 129 digital content providers that indicate in their reply to the sector inquiry that their services is available in at least two Member States, 117 replied to the question

whether they offer different catalogues of content in the different Member States where they make their services available. As follows from Figure C. 36 below, 38 % of those 117 respondents indicate that there were differences in the catalogue of content offered in each Member State.

Figure C. 36: Proportion of respondents whose catalogues of content services differ between the Member States and whose services are accessible in more than one Member State



(735) Catalogue differences may have different reasons when it comes to different content categories. General reasons for catalogue differences are differences in consumer taste and demand, as well as the relevance or not of certain content for certain territories. Some respondents also indicate that the need to negotiate with a multitude of right holders in order to be able to offer the same content in several Member States, which implies too important financial investments and resources.

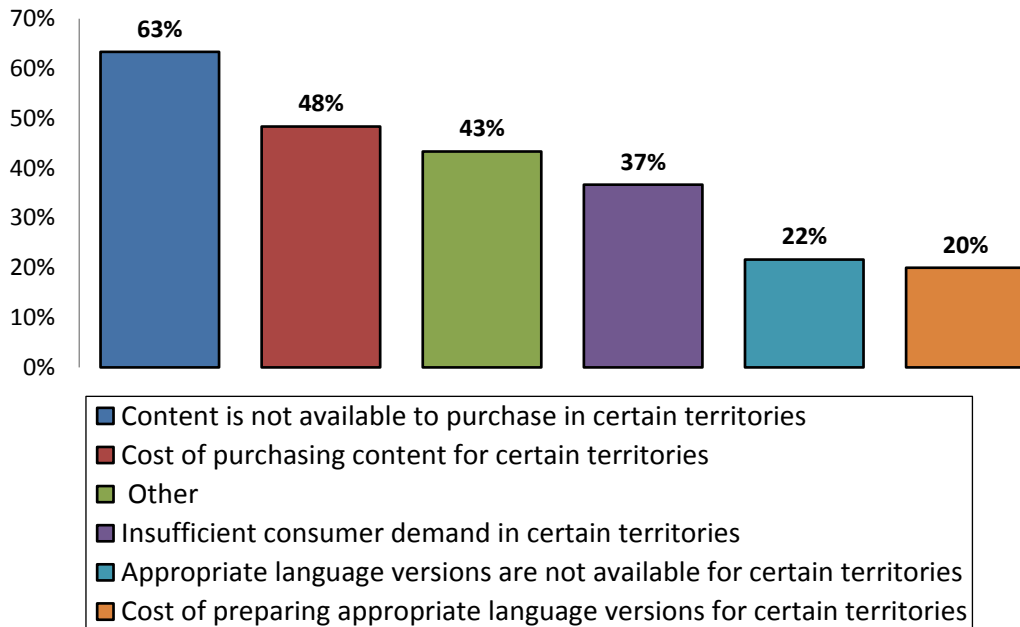
4.6 Reasons for catalogue differences

(736) Respondents were asked to provide the reasons for them offering different catalogues in different Member States. They were asked to choose between 5 given reasons or to choose "other" and if so to explain that choice. Figure C. 37 below shows that the main reason given by respondents for providing different catalogues to users in different Member States is that the rights in certain content are not available for licensing in respect of certain territories. The second main reason that was provided is the cost of licensing the content for certain territories.

(737) Some respondents to the questionnaire further explain the reasons why content may not be available to purchase or licence in certain territories. According to these respondents, the fact that rights are licenced on an exclusive basis to only one or possibly a few distributors that might distribute using different technologies in each Member State, makes it difficult for other operators or potential competitors to obtain the rights in

order to enter certain Member States or certain market segments in those Member States.

Figure C. 37: Reasons provided by digital content providers to catalogue differences between Member States - EU 28



(738) Several respondents (43 %) indicated that there were "other" reasons than those given in the questionnaire why they offer different catalogues of digital content in different Member States. Examples of reasons put forward are that rights are licensed on a national basis and may differ from one Member State to another as well as the existence of territorial restrictions based on contractual clauses.

(739) Catalogue differences may depend on the fact that right holders may have licensed the same content to another digital service provider, or that they may not hold the same rights in each Member State. Digital content providers have explained that to obtain the rights enabling them to offer the same catalogue in all the Member States in which they are active may require a too important investment in terms of cost and resources.

(740) Some respondents have also referred to the difficulty to compete in certain territories with other digital content providers in order to obtain access to content that is licenced on an exclusive basis. Moreover, the volume and cost of a certain content package are mentioned as important parameters on the basis of which digital content providers compete for specific titles that are part of the package.

4.7 Reasons provided by right holders why online rights are not licensed for certain territories

(741) There may be several reasons why a right holder chooses not to licence the online rights in certain content to digital content providers in some Member States. Obvious reasons include the commercial strategies and choices of right holders. This may result in online

rights for a certain territory not being available because the right holder has already licensed them on an exclusive basis to someone else.

(742) Some right holders explain that a pan-EU distribution arrangement with one distributor is less valuable both for the original right holder and subsequent licensors in the distribution chain, in terms of viewership and revenues, than licensing on a territorial basis to a couple of digital content providers. Therefore, they prefer to licence on a territorial basis.

(743) Other respondents explain that they may choose not to licence in certain Member States because of the commercial and territorial scope of the activities pursued by certain digital content providers with whom they may have long standing relationships. Where these digital content providers mainly distribute the licensed products in one or two Member States, they will not ask for a licence with a broader geographical scope. Some right holders also indicate that certain territories are not covered by a specific licensing agreement for a product because the rights were pre-sold in those territories.

(744) Other reasons mentioned are linked to consumer preferences and also the fact that productions are targeting certain territories for linguistic reasons (e.g. that dubbed versions do not exist). Moreover, certain territories may not have been offered to a certain digital content provider because the right holder had a more interesting offer for those territories from another provider.

4.8 Geo-blocking of digital content services

(745) In order to limit the online transmission of digital content to certain Member States and to implement (exclusive) territorial licensing agreements, digital content providers have recourse to geo-blocking measures.³⁴⁰

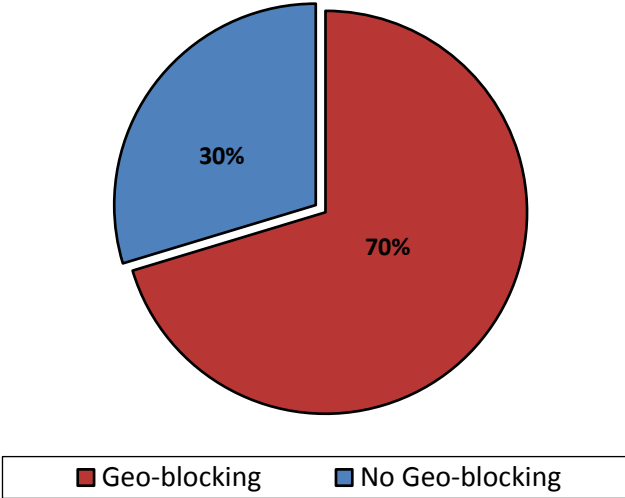
4.8.1 Existence and extent of geo-blocking

(746) In order to determine whether geo-blocking in relation to digital content takes place, digital content providers were asked to specify whether they had put in place technical measures to monitor the user's location in order prevent access to their services.

(747) The responses to these questions were aggregated so that any respondent indicating the use of at least one technical measure was considered as carrying out geo-blocking, and this aggregated number of respondents carrying out geo-blocking was divided by the total number of respondents, providing the percentage of respondents that actively geo-block. As can be seen from Figure C. 38, geo-blocking is widely used across the EU.

³⁴⁰ As mentioned above (see footnote 187), in the framework of the sector inquiry, the Commission published in March 2016 its initial findings on geo-blocking in an Issues paper (See SWD(2016) 70 final). The initial findings of the Issues paper are confirmed by the Preliminary Report. However, as the Commission received some of the responses only after the data extraction date for the Issues paper, certain figures have been slightly modified.

Figure C. 38: Proportion of respondents implementing at least one type of geo-blocking measure – EU 28

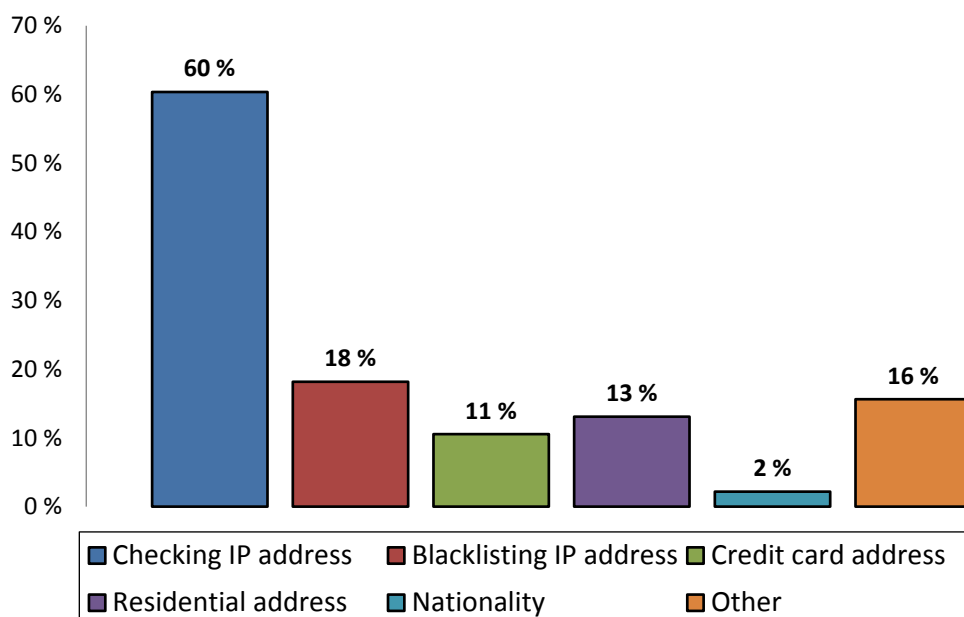


(748) Respondents were asked about the technical means used to implement geo-blocking to prevent access to their offer by users located in Member States other than the one where the service provider is established.

(749) As Figure C. 39 shows, most respondents use IP address verification which is the prevalent form of technical implementation by a wide margin.³⁴¹

³⁴¹ The relatively high proportion of respondents that answered "Other" is due to two reasons. First, technical measures that were genuinely different from the options provided were specified by some respondents, together with the indication of such means, including for example the use of telephone area codes or the use of content encryption to enable geo-blocking. However the majority of the respondents specifying "Other" indicate that they use a combination of the methods listed, or that they provide more than one service and geo-blocking applies only to a sub-set, or do not specify what technical measure they use.

Figure C. 39: Technical measures used to implement geo-blocking – Average proportion of all respondents – EU 28



(750) The EU average masks a relatively high degree of variation, both across Member States and across types of operators.

(751) In particular, geo-blocking measures are reported to be used more widely in certain Member States. While no clear pattern emerges from the data, only in Estonia (33 %) and Italy (46 %) do less than half of respondents in Member States use such measures.³⁴²

(752) By contrast, more than half of the respondents use such measures in Spain (65 %) and the Netherlands (67 %), while more than three quarters of respondents use such measures in France (81 %), the UK (83 %), Denmark (86 %) and the Czech Republic (87 %).

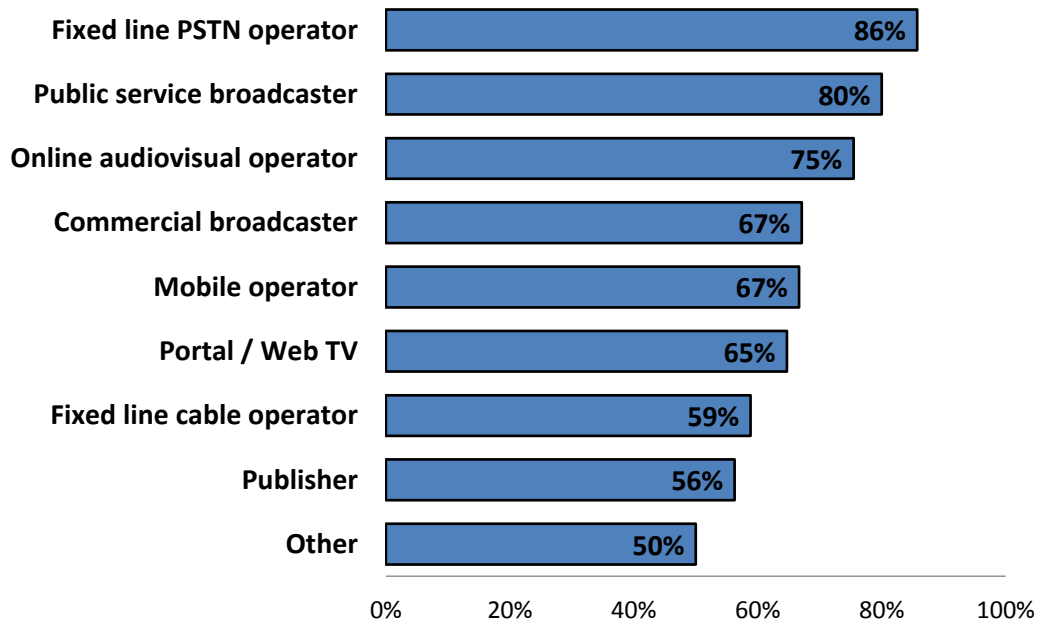
(753) The gathered data indicate a relatively wide degree of variation also across respondents, independently of their geographic establishment, as illustrated by Figure C. 40.

(754) For example, online audiovisual operators and fixed telephony operators make on average a more extensive use of geo-blocking than commercial broadcasters do. A high proportion of public service broadcasters implement some form of geo-blocking.

(755) Fixed line cable operators resort less to geo-blocking than other fixed line communications providers, but this may be partly a result of the fact that subscribers typically need to be physically connected to the specific cable network to receive a complete service, in which case geo-blocking might be unnecessary.

³⁴² The results may also be affected by the different size of the respondent sample in each of the Member States.

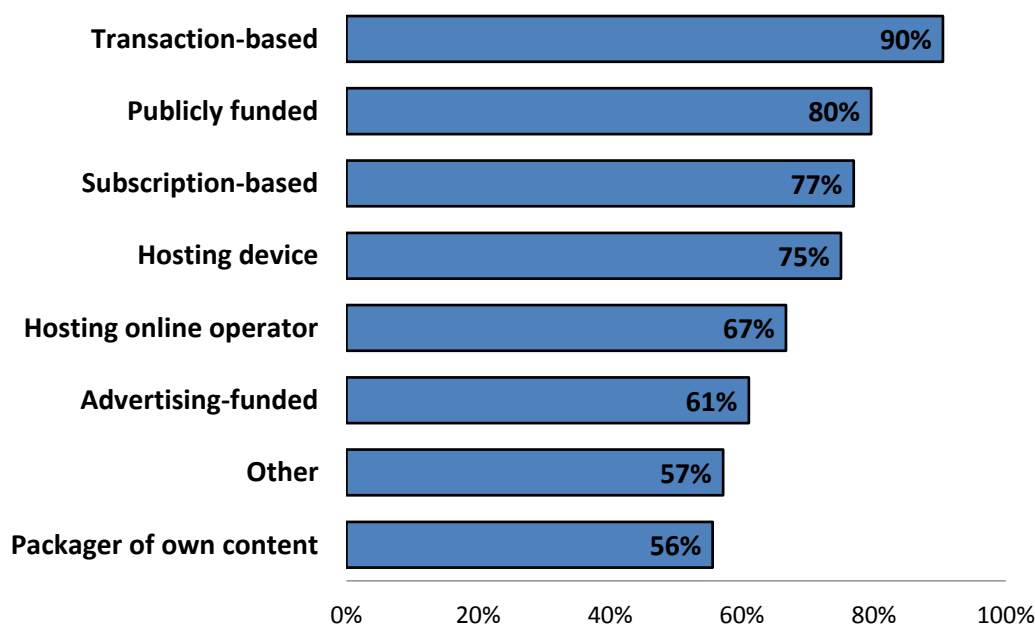
Figure C. 40: Proportion of digital content provider respondents implementing at least one type of geo-blocking by type of operator – EU 28



(756) Similarly, there is also high variation in the extent to which technical geo-blocking measures are deployed when looking at the different types of business models. Figure C. 41 presents data that indicate that the average majority of respondents offering paid services, regardless of whether they are offered pursuant to a transaction- or a subscription-based model, deploy technical geo-blocking measures aimed at limiting cross-border access.

(757) Conversely, operators that adopt a business model centred on advertising sales, as well as those which earn most of their revenues from selling packaged content (possibly to retailers, rather than directly to users), make on average less use of geo-blocking than other operators.

Figure C. 41: Proportion of digital content provider respondents implementing at least one type of geo-blocking by business model – EU 28



4.8.2 Geo-blocking required by licensing agreements

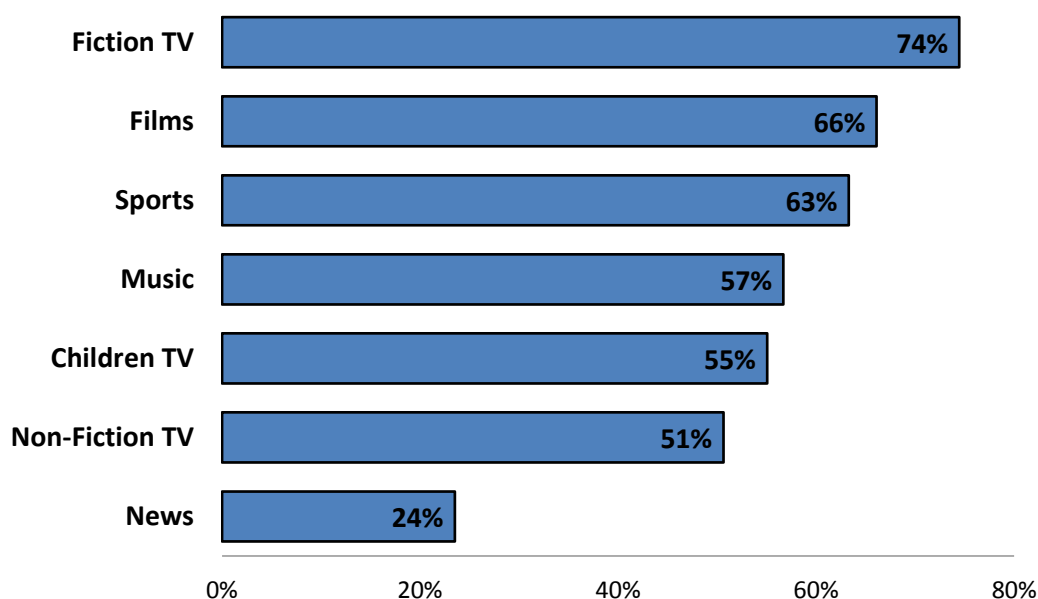
(758) Respondents were asked whether the licensing agreements they have in place with right holders include the requirement to apply geo-blocking measures to prevent access from users located in Member States other than those where the respondent was providing the service.

(759) In particular, the agreements were sub-divided into seven types of products (see paragraphs (616) and onwards) and respondents were asked to include information on the 30 largest suppliers of content for each of these categories.

(760) All agreements that included a requirement for digital content providers to geo-block their service were subsequently aggregated, regardless of the technical implementation of geo-blocking. The extent to which geo-blocking is required as a proportion of the total number of agreements and by category of digital content³⁴³ is reported in Figure C. 42.

³⁴³ Respondents were asked to provide the information per supplier. Therefore, while at the level of each individual respondent the information obtained is per supplier, over the whole sample, there may be a duplication of suppliers across respondents. One could in this case consider the above results as being based on the number of "contractual relations" or "agreements."

Figure C. 42: Proportion of agreements requiring providers to geo-block by category – Average for all respondents – EU 28



(761) For example, 74 % of all licensing agreements with suppliers of television fiction submitted by digital content providers require them to geo-block. Licensing agreements for TV drama and TV series, and films and sports events, include requirements to geo-block more often than licensing agreements for other digital content categories.

(762) However the average results mask a high degree of variation.

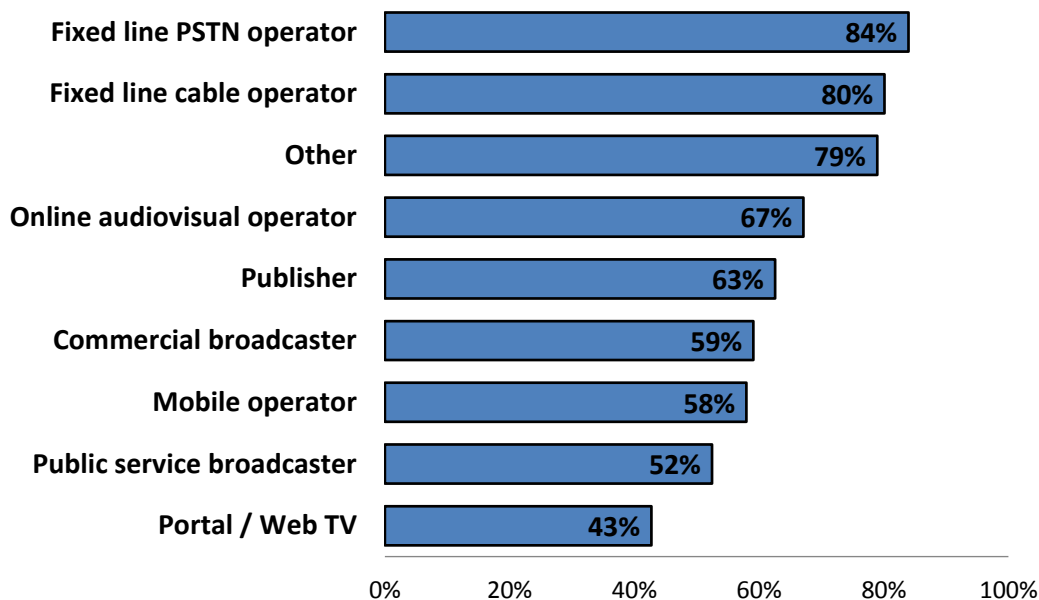
(763) First, respondents in several Member States highlight differences in the prevalence of contractual geo-blocking requirements compared to the average. Agreements on the licensing of digital content such as films, sports and TV series are not in every Member State the ones where the highest degree of geo-blocking is contractually required.

(764) Second, there is a high degree of variation in the extent to which geo-blocking is required for the same category of content. This seems to point to the existence of different business models or different market characteristics.

(765) Looking at the contractual restrictions for each type of operator, Figure C. 43 can shed further light on the differences. In particular, fixed line operators have the highest proportion of agreements requiring geo-blocking. Compared to Figure C. 40, public service broadcasters face fewer contractual restrictions than it would appear from the extent to which they resort to geo-blocking. This might be linked to the fact that a large part of the digital content they offer is produced by them and licensed intra-group, and thus may not need to impose geo-blocking contractually as a measure to restrict access. Another reason why they then resort to geo-blocking unilaterally may be that they do not have the full range of rights needed to engage in online retransmission of their programmes.

(766) Overall, 59 % of digital content providers are contractually required to geo-block by their suppliers, i.e. right holders.

Figure C. 43: Proportion of agreements requiring digital content providers to geo-block by type of operator



4.8.3 Geo-blocking measures used to restrict cross border access and portability

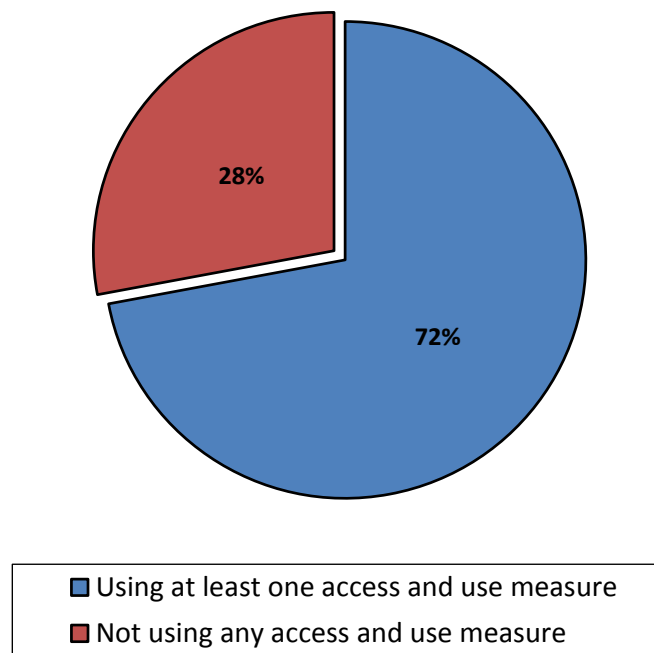
(767) Access and portability restrictions are for the purpose of this Preliminary Report defined as technical geo-blocking measures which restrict the ability of users to access and use content from outside the territory of their Member State.

(768) Respondents were asked whether the technical measures that they apply have any impact on:

- (a) The user's ability to play previously downloaded content in certain territories;
- (b) The catalogue of content and/or services available to a given user in different territories; and
- (c) The ability of an existing user to access the service in different territories.

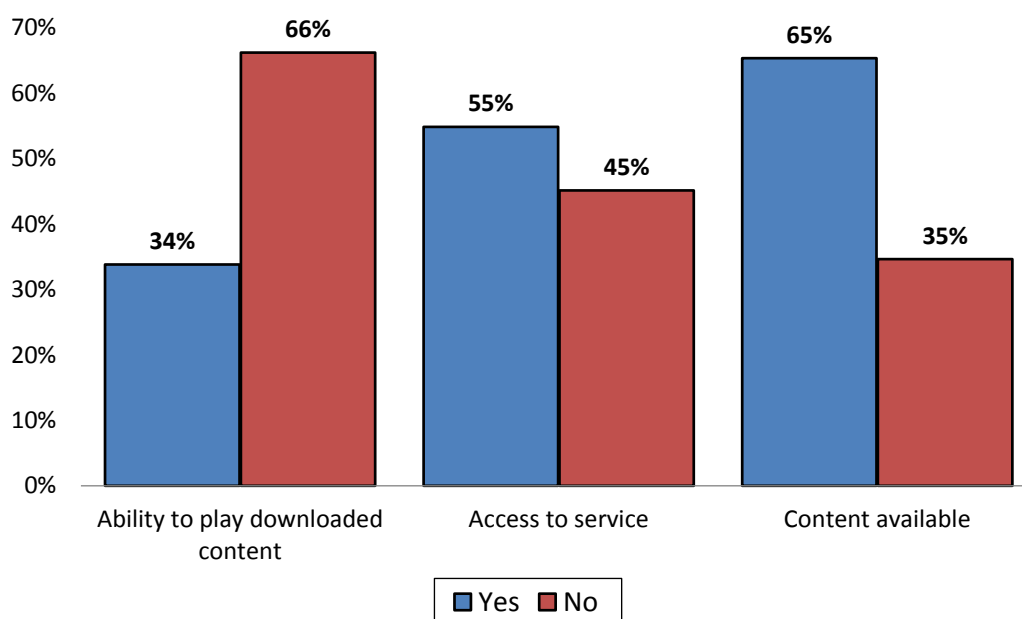
(769) As follows from Figure C. 44 below, the replies by digital content providers indicate that access and portability restrictions are frequently used. 112 of the respondents to this question, corresponding to 72 %, indicate that they apply at least one of the three above-mentioned types of restrictions. 44 respondents, corresponding to 28 %, state that they do not apply any of the three above-mentioned access and portability restrictions.

Figure C. 44: Proportion of digital content providers that use technical geo-blocking measures to restrict users' access to and use of digital content



(770) The most common restriction consists of limiting the catalogue of content and accessible services in different Member States. A majority of respondents (65 %) to the above-mentioned question indicate that geo-blocking measures are used to restrict the content and services made available in different Member States, which leads to different content catalogues being offered to users in different territories. A number of respondents also indicate that the restrictions in place affect the ability of an existing user to access the service from certain territories (55 %). A restriction of the users' possibility to play previously downloaded content in certain Member States is less frequently used. 34 % of the respondents indicate that they use technical geo-blocking measures to restrict a user's ability to play previously downloaded content in certain territories.

Figure C. 45: Proportion of content providers that use technical geo-blocking measures to restrict users' access to and portability of digital content – Per type of restriction



4.8.4 Restrictions on access and use in the terms of service for users

(771) In addition to being asked whether they use geo-blocking measures to prevent or restrict access to and use of digital content, digital content providers were also asked whether they restrict users' possibilities to e.g., access content or to play downloaded content in some Member States, through their terms of service.

4.8.4.1 Unilateral restrictions on access and use in the terms of service for users

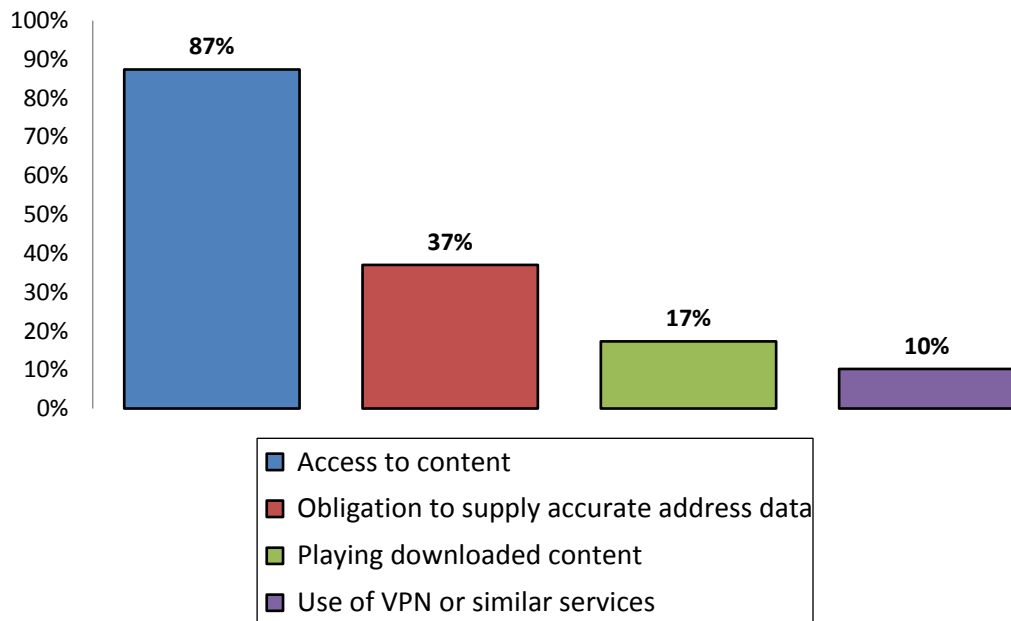
(772) As regards unilateral restrictions imposed on users by digital content providers through their terms of service, digital content providers were more precisely asked whether their terms of service contain any provisions concerning:

- (a) The user's right to access content in certain territories;
- (b) The user's right to play downloaded content in certain territories;
- (c) The user's right to access content through VPN and other services that can make it difficult to determine the user's location; or
- (d) The user's obligation to supply accurate address data when signing up for an account or a subscription.

(773) As follows from Figure C. 46 below, 87 % of the respondents to that question replied that their users' terms of service contain restrictions as to the users' possibility to access content. In addition, around a third (37 %) of the respondents requires the user to supply accurate data when signing up for an account or a subscription.

(774) 10 % of digital content providers do moreover restrict users' right to access content through VPN or other similar services. The replies received to the questionnaires show that some digital content providers do out of their own initiative restrict or prohibit their users to deploy VPN or similar services, and not because they are required to do so by right holders.

Figure C. 46: Proportion of digital content providers that restrict users' access to and use of digital content through their terms of service – All digital content providers



(775) Some respondents have indicated that they have received questions and comments from right holders or other distributors of content concerning the effectiveness of the technical measures they use to ensure that content is not accessed outside the territory or territories for which they hold a licence. Comments were received both during the negotiations of the licensing agreements and thereafter, and both orally and in writing.

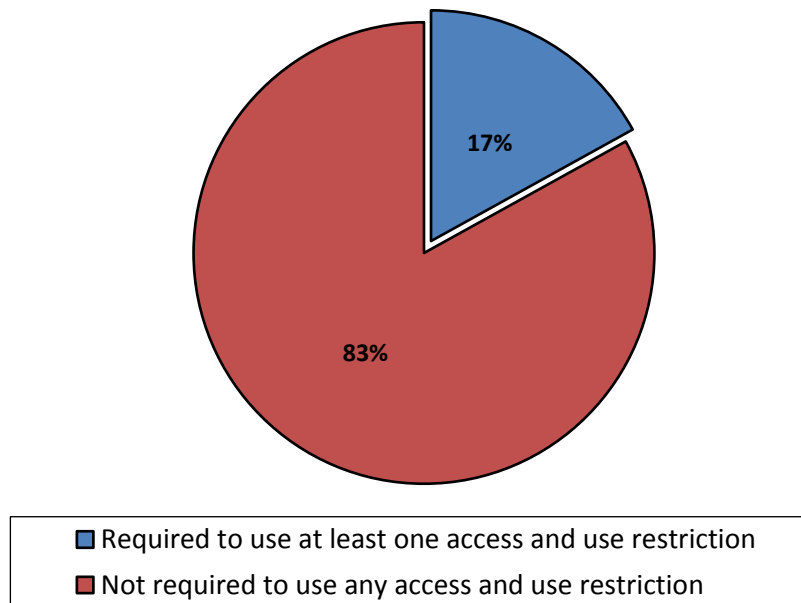
4.8.4.2 Contractual restrictions on access and use in the terms of service for users

(776) Digital content providers were also asked whether their terms of service contain access and use restrictions because the licensing agreements with right holders require them to include such provisions in their terms of service. In particular, respondents were asked to indicate whether they were required to include provisions in their terms of service concerning one or more of the following issues:

- (a) The Member States in which users can access content;
- (b) The Member States in which users can play downloaded content; and
- (c) The possibility for users to access content through VPN or similar services that can make it difficult to determine the location of the user.

(777) According to Figure C. 47 below, 83 % of the licensing agreements submitted by digital content providers require them to include at least one of the above-mentioned restrictions in their terms of service.

Figure C. 47: Proportion of licensing agreements requiring digital content providers to include provisions on access and use in their terms of services – All agreements submitted by digital content providers



(778) According to Figure C. 48 below, almost all respondents (93 %) indicated that they are required on the basis of the licensing agreements that they have concluded with right holders to include provisions in their terms of service concerning the Member States in which users may access the content. It is in general less common that the licence agreements require the digital content providers to indicate to the users in which Member States downloaded content may be played. In 22 % of the submitted agreements digital content providers are required to indicate in their terms of service where the users may play downloaded content.

(779) A small minority of respondents (3 %) have replied that right holders require on the basis of the licensing agreements that their terms of service must contain rules concerning the users' access to content via VPN or similar services. Such provisions are only required in relation to the following types of content: fiction TV, children TV, films and music. Figure C. 48 indicate that they are the most common in relation to fiction TV (5 %) and film (6 %) content, but still remain rare.

(780) Figure C. 49 shows that the most frequent restriction throughout all content types is a restriction of the Member States in which the user can access digital content. Restrictions as to the Member States in which users can play downloaded content are overall less frequent and are present mainly in agreements concerning films, sports, fiction and children TV content.

Figure C. 48: Proportion of licensing agreements requiring digital content providers to include provisions on access and use in their terms of services – All agreements submitted by digital content providers

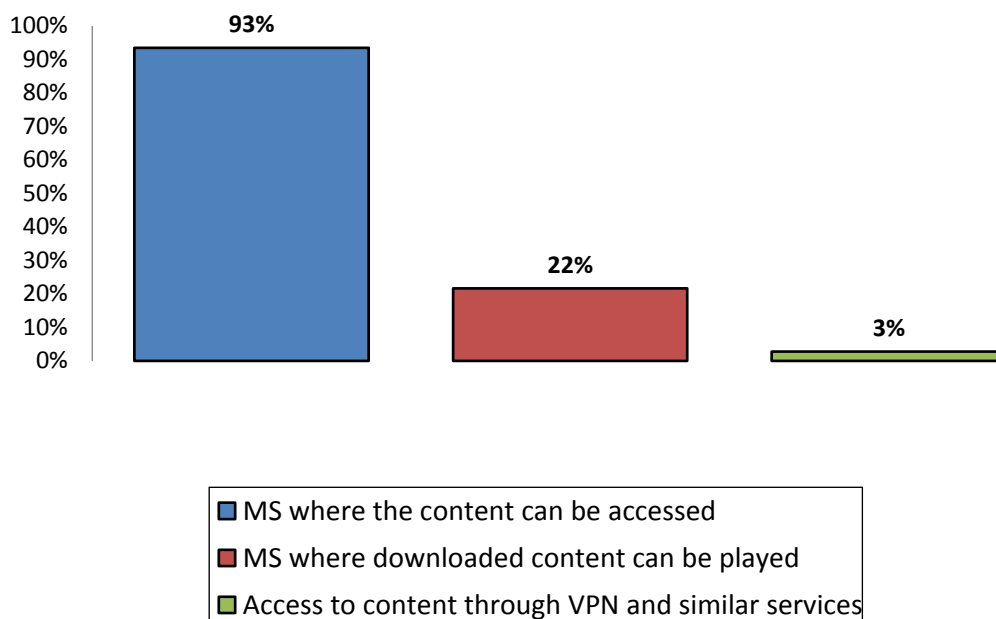
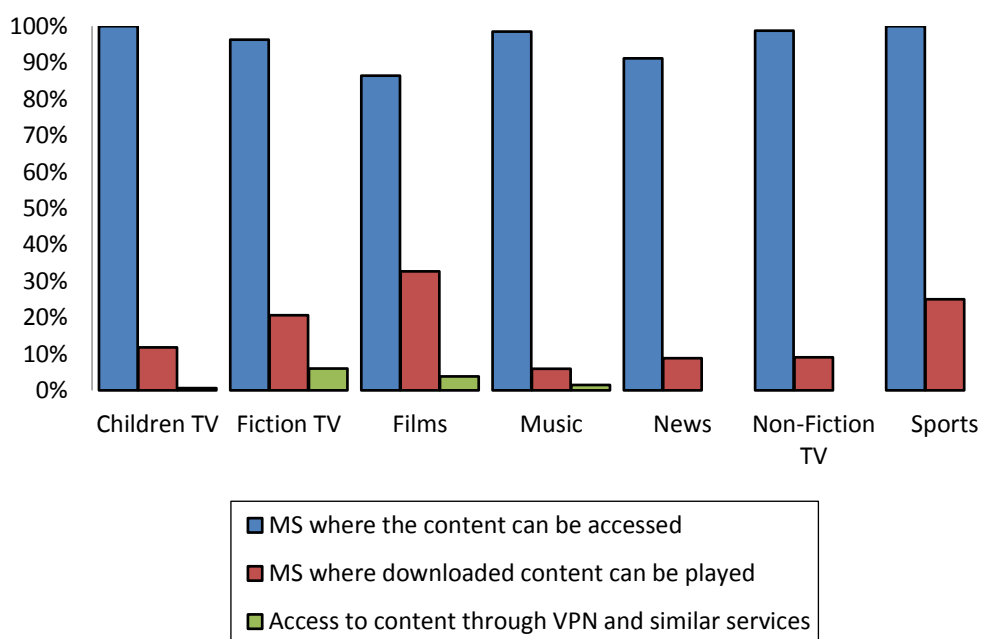


Figure C. 49: Proportion of agreements requiring digital content providers to include provisions on access and use in their terms of services – Agreements submitted by digital content providers by type of content



4.9 Contractual provisions concerning monitoring, sanctions and compensation in relation to geo-blocking

(781) In order to monitor the application and implementation of technical geo-blocking measures, right holders include clauses in licensing agreements in order to verify or audit the way such measures are applied or whether they meet the required standards of geo-blocking. Some agreements also enable right holders to impose sanctions or ask for

compensation in the event the digital content provider does not comply with technical geo-blocking measures or with the provisions defining the territorial scope of the licensing agreement.

(782) It follows from the sections below that a large majority of the submitted agreements include both monitoring clauses and provisions on sanctions and compensation.

4.9.1 Monitoring provisions

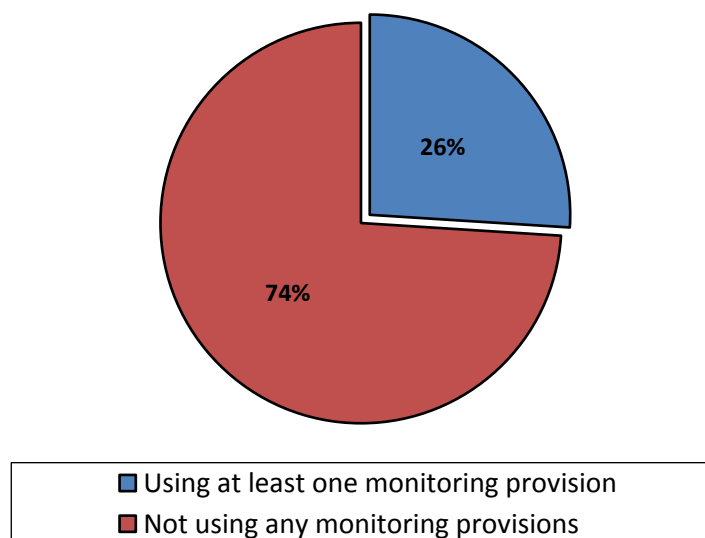
(783) As regards the use of clauses enabling right holders to monitor the implementation and use by digital content providers of technical geo-blocking measures, digital content providers were asked whether their licensing agreements with right holders contain such provisions as well as provisions requiring them to take certain actions to keep the right holder informed of the use of geo-blocking measures. Digital content providers were more precisely asked whether the licensing agreements contain provisions requiring them to:

- (a) Inform the right holder of specific technical geo-blocking measures and methods used;
- (b) Submit data to the right holder concerning the use of technical measures;
- (c) Allow the right holder to audit the technical measures used;
- (d) Change the technical measures that the right holder finds insufficient.

(784) In addition to the above options, respondents could also reply that there were "other" types of provisions and were asked to explain their reply.

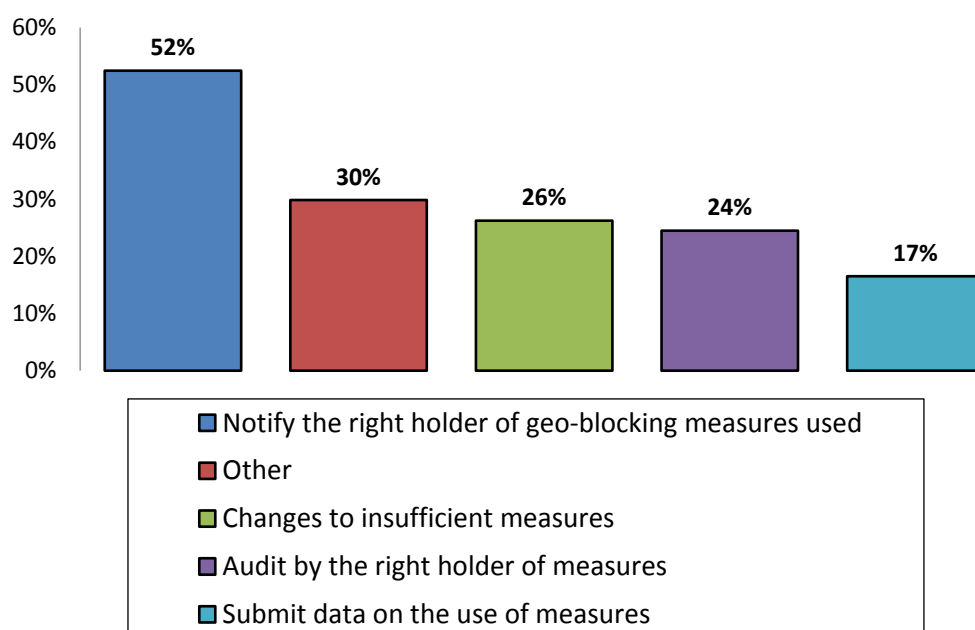
(785) As stated above, monitoring provisions are frequent features of licensing agreements. According to Figure C. 50 below, 74 % of the licensing agreements submitted by digital content providers contain at least one of the above-mentioned monitoring provisions.

Figure C. 50: Proportion of licensing agreements that include at least one monitoring provision – All agreements submitted by digital content providers



(786) It follows from Figure C. 51 below that the most common monitoring provision that can be found in the licensing agreements submitted by digital content providers is an obligation to notify the right holder of the specific methods or measures used to geo-block. 51 % of these agreements contain such an obligation. The second most common requirement that is present in 32 % of the agreements, is the obligation to allow the supplier to audit the technical geo-blocking measures used.

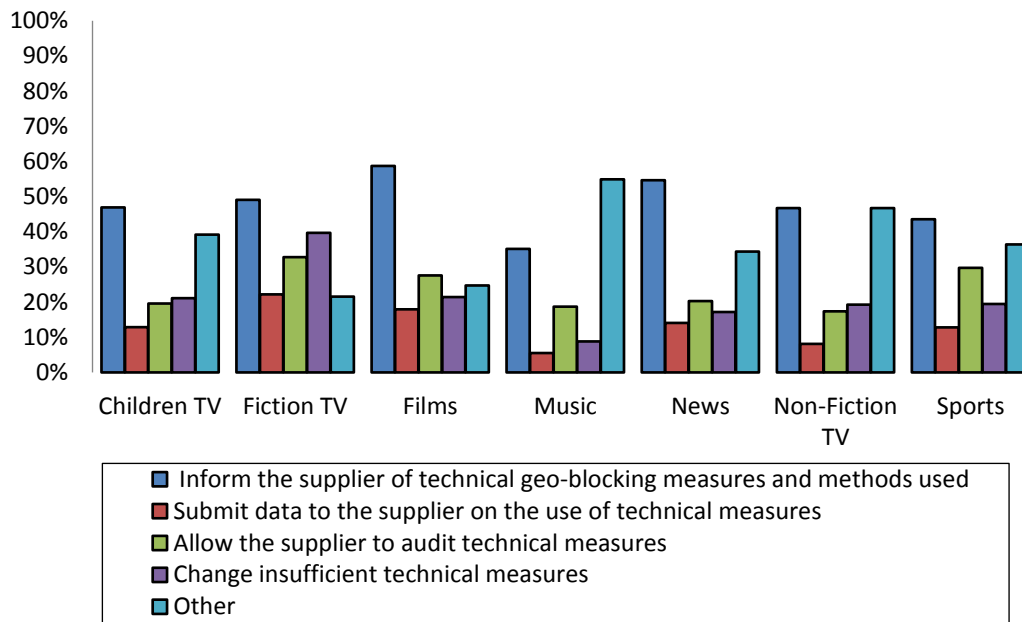
Figure C. 51: Proportion of different monitoring provisions contained in licensing agreements – All agreements submitted by digital content providers



(787) Figure C. 52 below shows that all the content types that were covered by the questionnaire to digital content providers contain all the four monitoring provisions. The

most common one is however the obligation to notify the right holder of the specific methods or measures used to geo-block. Except for music content, around half of the licensing agreements contain such a provision. The second most common requirement, throughout all the seven content categories, is the obligation to allow the supplier to audit the technical measures used.

Figure C. 52: Proportion of licensing agreements that contain monitoring provisions - Agreements submitted by digital content providers - Per content type



(788) Many respondents in each of the content categories have however replied that the licensing agreements contain "other" provisions concerning monitoring. Several respondents indicate that the licensing agreements oblige them to inform the right holders of any unauthorised use of content or any breach of its security and copy control systems, of use of hacking or other pirating software or any other means of circumventing geo-blocking measures as well as the number of catch-up users, the number of views that last for a certain minimum time. Other agreements provide that both contracting parties are obliged to inform each other of any transmissions of content outside the licenced territory.

(789) Respondents also indicate that some agreements enable right holders to technical audits of the digital content provider's' services and functions such as storage, hosting, security, performance, display and delivery. Certain agreements moreover give right holders the right to inspect and review the digital content providers' facilities and security systems.

(790) Certain licensing agreements provide that the technical geo-blocking measures used must be the latest on the market and shall be at least as efficient as those used by the digital content provider to protect other right holders' content. Some agreements moreover provide for an obligation to regularly review the effectiveness of geo-blocking technologies used and to upgrade them where necessary. In order to change the

permitted technical geo-blocking measures or other security solutions used, the right holder's written consent is often required.

4.9.2 Sanctions and compensation for non-compliance with territorial and geo-blocking clauses

(791) In addition to monitoring provisions, licensing agreements may also provide for a right for the right holders to request that the digital content providers suspends distribution of content and/ or to ask for compensation in the event the digital content provider does not comply with technical geo-blocking measures or with the provisions defining the territorial scope of the licensing agreement.

(792) The Commission asked digital content providers whether their current agreements with right holders contain provisions allowing the right holder to request that distribution of content is suspended in the following situations:

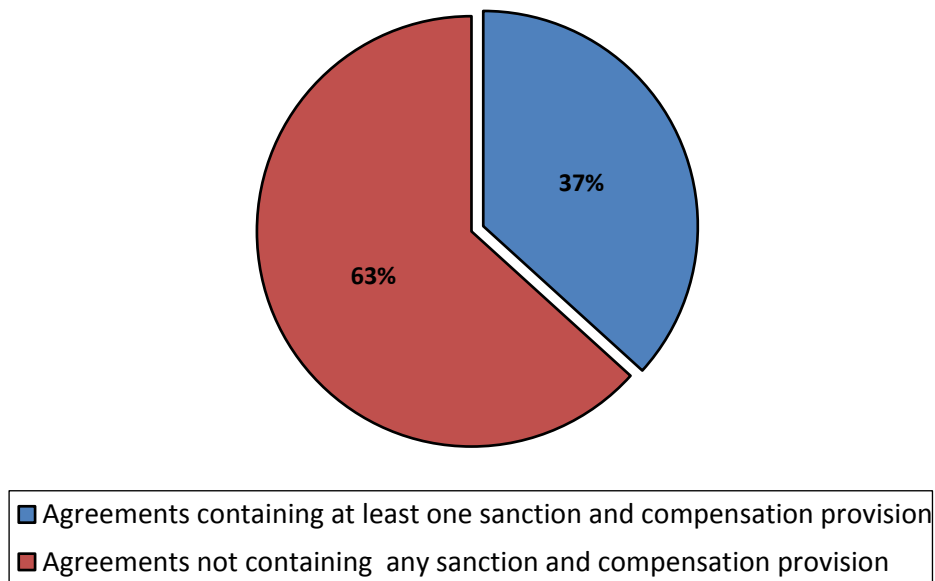
- (a) with immediate notice if the digital content provider does not comply with territorial clauses;
- (b) with immediate notice if the digital content provider does not comply with technical geo-blocking measures;
- (c) after agreed verification if the digital content provider does not comply with territorial clauses;
- (d) after agreed verification if the digital content provider does not comply with technical geo-blocking measures.

(793) Digital content providers were also asked whether their current agreements with right holders contain provisions allowing the right holder to ask for compensation in the following cases:

- (a) if the provider does not comply with territorial clauses;
- (b) if the provider does not comply with technical geo-blocking measures.

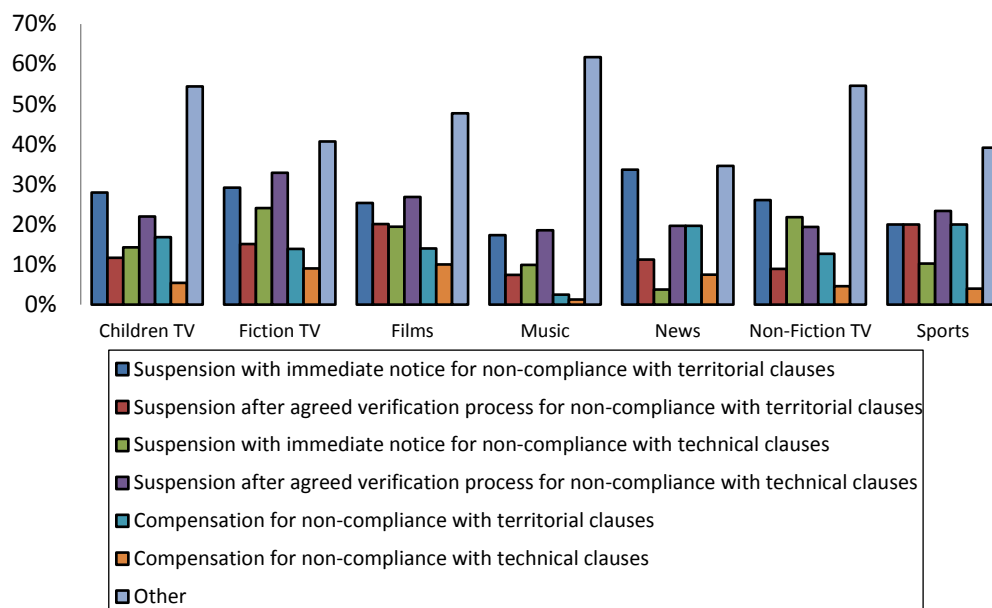
(794) According to Figure C. 53, a majority of the licensing agreements submitted by digital content providers (63 %) contain at least one of the above-mentioned provisions.

Figure C. 53: Proportion of licensing agreements that contain at least one provision on sanctions and compensation – Agreements submitted by digital content providers



(795) Figure C. 54 below shows that the provisions on sanctions and compensation contained in the licensing agreements with right holders vary depending on the type of content. However, the most common provisions according to the respondents are those that provide for the suspension of the licensing agreement with immediate notice where the digital content provider has not respected territorial restrictions, and those that provide for suspension for non-compliance with technical restrictions, after an agreed verification process has been completed. Suspension of the distribution of certain titles or products may occur when the right holder becomes aware the title or product has been distributed in a territory not covered by the licensing agreement, for example following complaints from digital content providers in other territories.

Figure C. 54: Proportion licensing agreements that contain provisions on sanctions and compensation – Agreements submitted by digital content providers – Per content type



(796) As follows from Figure C. 54, a rather large proportion of the respondents indicate, for each of the content types represented in that figure, that their agreements contained "other" types of provisions concerning verification, sanctions and compensation than the given ones.

(797) Respondents explained that such "other" types would be provisions allowing right holders not only to suspend the distribution of content but also to terminate the agreement in case of breach of the contractual obligations. Respondents indicate that in such cases, the agreement often provides for a possibility for the digital content provider to remedy the breach within a certain time-period before the right holder has the right to terminate it.

(798) Respondents also indicate that provisions that provide for compensation do in general apply to any breach of the agreement and are not limited to non-compliance with territorial restrictions or technical geo-blocking measures. The amount of compensation to be paid to the right holder in such cases seems to vary largely. A couple of respondents indicate that the amount would equal the licensing fees to be paid on the basis of the agreement during the remaining duration of the agreement.

4.10 Use of VPN and IP routing services

- (799) The Commission contacted several providers of VPN³⁴⁴ and IP routing services. These services are typically used by individuals and/or organisations that seek to achieve a higher level of privacy in their communications on the internet.
- (800) VPN and IP routing services are in principle capable of masking, hiding or replacing the real IP address of the user that makes use of them. It is therefore possible that users may use these services to bypass geo-blocking by digital content providers. Many VPN or IP routing services are established outside of the EU and most of them make use of infrastructure (i.e. mainly servers and leased lines) that are located around the world.
- (801) Virtually all respondents to the VPN questionnaire pointed out that they do not collect any type of information on the identity or location of users, nor do they monitor the content of the communications between the user and any other user or service provider.
- (802) The 9 VPN and IP service providers that responded have between 20 000 and more than 100 000 regular users in the EU, a large majority of whom access their services regularly (between every day and three times a week). Most respondents pointed to substantial growth rates in the number of users.
- (803) Three respondents said that up to 20 % of the traffic generated by users on their service is likely to relate to video, audio or audio-visual streaming, while two said it was between 21 and 40 % and one between 61 and 80 %. It is not possible, however, to determine the extent to which such traffic relates to accessing commercial digital content services.

Summary

A majority of online digital content seems to be made available to users prevalently on a national basis, or for a territory covering two to four Member States, in the latter case when they share a common language. The main reasons why digital content providers do not make their services available in other territories are the cost of purchasing content for territories in which the digital content provider is not yet active, and that the rights for the content is not available for licensing in some territories. Digital content providers that make their services available in two or more Member States do not necessarily offer the same catalogue of content in each of those Member States. The main indicated reason for differences in catalogue between different Member States is that the same rights are not always available for licensing in all the Member States where the digital content provider is active.

Geo-blocking is widely used by respondents across the EU. 70 % of digital content provider respondents restrict access to their online digital content services from other Member States. However responses suggest relatively large differences in the extent to which geo-blocking is

³⁴⁴ Virtual Private Network, i.e. an encrypted communication channel that can be established between two computers or IP-based devices.

used both between different types of business models and between Member States. In some Member States (e.g. Italy) only a minority of respondents use geo-blocking while in others (e.g. UK) the majority of respondents do so. Geo-blocking also appears to be more used by certain operators than others. Geo-blocking appears to result from contractual restrictions in licensing agreements between digital content providers and right holders. Almost 60 % of digital content provider respondents are contractually required by right holders to geo-block, and the majority of licensing agreements submitted include such requirements for all product types, except for news products. Geo-blocking is most prevalent in agreements for films, sports and TV series.

Most digital content providers are also required to include restrictions in their terms of service concerning the Member States in which users may access content. Licensing agreements do moreover enable right holders to monitor digital content providers' use of geo-blocking measures or compliance with territorial restrictions, or to impose sanctions and ask for compensation where such measures or territorial restrictions are not complied with.

5. THE SCOPE OF LICENSED RIGHTS: RELEASE WINDOWS

(804) The release of many content products is staggered across different release periods (so-called "windows" or "windowing"). The importance of the release window system and holdback clauses is confirmed both by the right holders' and digital content providers' responses.

(805) Release windows are contractually enforced through the so-called "holdback clauses" which preclude the distribution over certain transmission technologies until certain period of time has passed. As will be further explored in section C.6, this is an additional dimension of exclusivity, i.e. temporal exclusivity. The length of each release windows is a matter of complex agreements between right holders and digital content providers.

(806) In particular, this complex mechanism entails that the value of any window is reduced if the following window is scheduled earlier. In other words, windowing is a pricing strategy and price tends to decrease as the product gets older.³⁴⁵

(807) The analysis of the release windows is complex, as windows are defined differently by different right holders and for different types of products. For example, in some instances (e.g. output deals), release windows differs according to the type of transmission technology (basic TV, SVOD, catch up) as well as the type of products. Licensing agreements may include multiple release windows, each of which governed by different rules.

³⁴⁵ There are significant exceptions to this rule, in particular for products that become "classics" or those that acquire a new lease of life when rediscovered by larger numbers of users. Such products can command higher prices, relative to products having an equivalent life span, despite (or more appropriately, in this case, thanks to) their longevity.

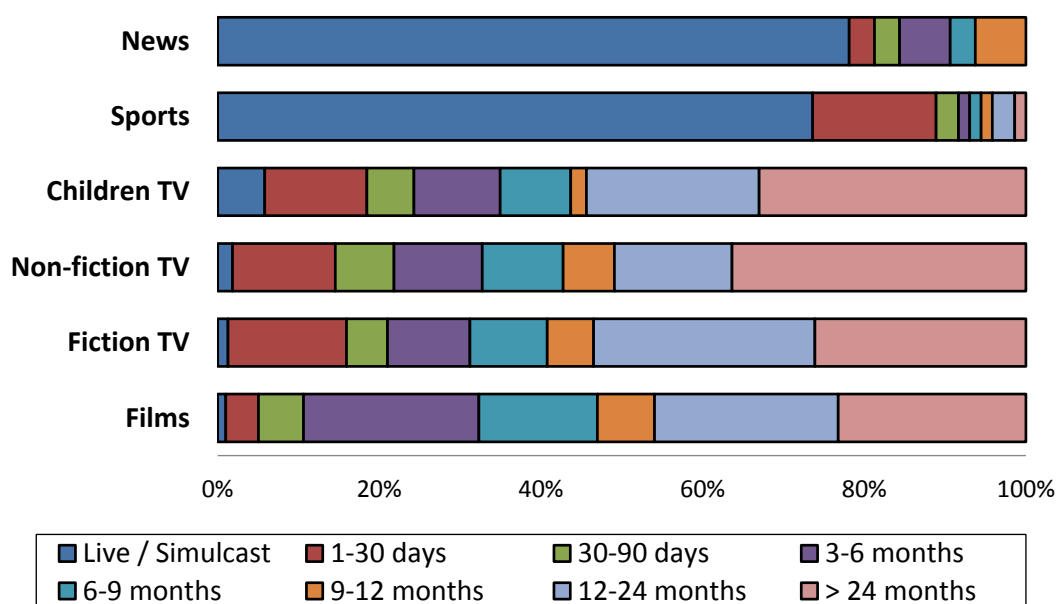
(808) It is also difficult to provide an overview of the different types of release windows given that they are subject to change and may differ between Member States. For most fiction products (i.e. films and television fiction) the pay per view (or video on demand) window tends to open between 3 and 6 months after the first commercial release of a product (i.e. the first time the product is commercialised in a given licensed territory), while the pay-TV window tend to open between 6 and 12 months after the first release. Normally, between 12 and 24 months after its first release the content might already have lost a relatively large part of its commercial value and, therefore, only at this point it is normally released on free-to-air TV.

(809) For other types of products, windowing can be different. In particular, sports and news products tend to loose attractiveness for users immediately after their first release, which tends to be the live broadcast of the sports event or news programme.

(810) Figure C. 55 shows the typical holdback periods applied to online content, according to the type of content. Holdback periods are pervasive in licensing agreements.

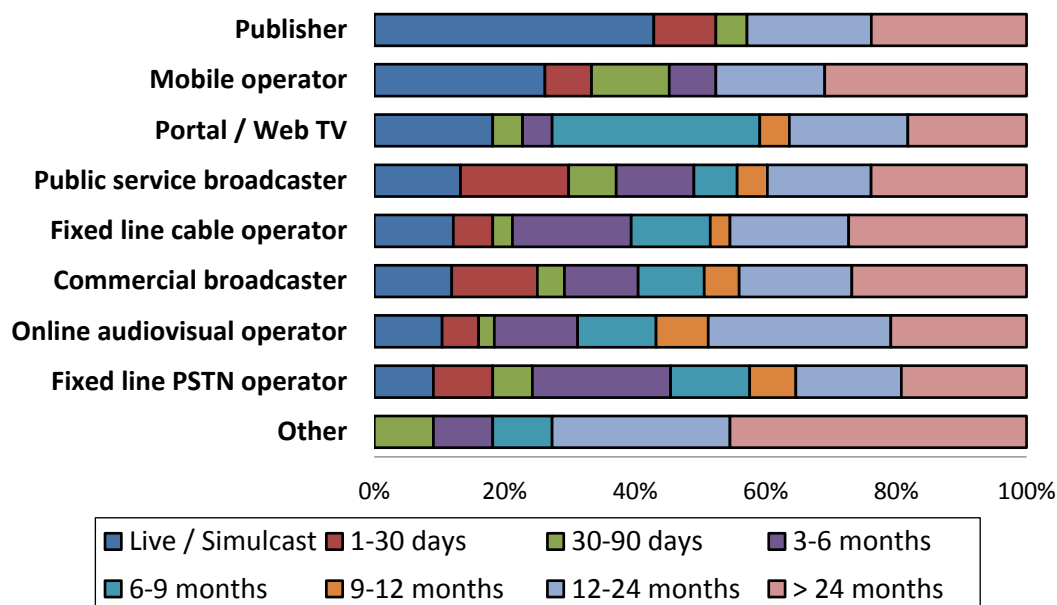
(811) The characteristics of each product determine the release windows. For news and sports products, as can be expected, live or simulcast releases are the most prevalent way to exploit the licensed right. For the other types of products, release windows are more rigidly defined, with increasingly shorter durations of the first windows.

Figure C. 55: Proportion of agreements including specific holdback periods by product type – All agreements submitted by digital content providers



(812) The same conclusion can be drawn if the data is broken down according to the type of operator, rather than the type of content (Figure C. 56). Agreements concluded by all types of operators contain the release windows system.

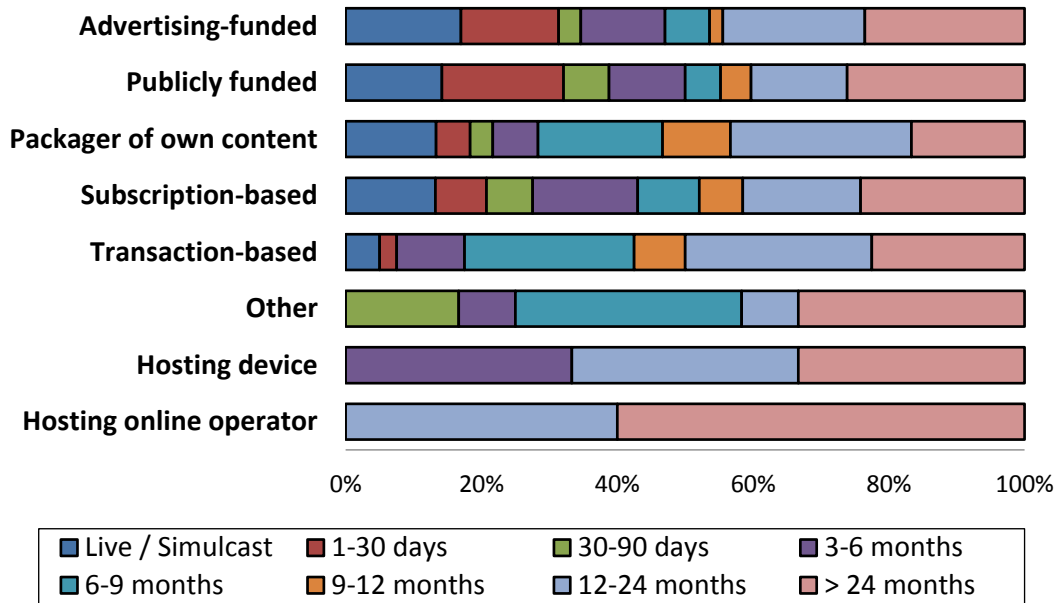
Figure C. 56: Proportion of agreements including specific holdback periods by type of operator – All agreements submitted by digital content providers



(813) Figure C. 56 above shows for each type of operator the proportion of agreements including given release windows. In this regard publishers seem to have the highest percentage of agreements including rights for the first release window. The smallest percentage of agreements including rights for first and second release windows concerns online audiovisual operators and fixed line telephone operators. This reflects their type of offer, centred on paid products for which the release window opens normally between 3 and 9 months after the first release.

(814) The breakdown of the data according to the digital content provider's business models also confirms the importance of the release windows system (Figure C. 57). Only hosting online operators do not seem to be particularly restricted by windowing. This might be explained by the fact that a large part of the content they offer is user-generated, and that the relevant rights may have not been acquired in advance from right holders due to that fact.

Figure C. 57: Proportion of agreements including specific holdback periods by business model – All agreements submitted by digital content providers



Summary

The release of many content products is staggered across different release periods (so-called "windows" or "windowing"). Release windows are contractually enforced through the so-called "holdback clauses" which preclude the distribution over certain transmission technologies until certain period of time has passed.

6 EXCLUSIVE RIGHTS IN CONTENT IN THE LICENSING AGREEMENTS BETWEEN RIGHT HOLDERS AND DIGITAL CONTENT PROVIDERS

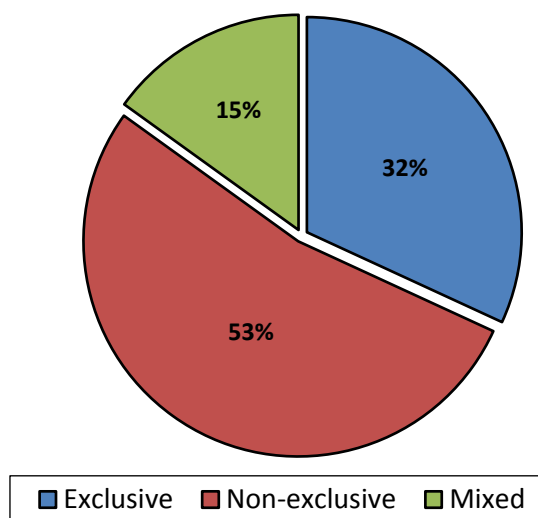
(815) As indicated in paragraph (626), rights may be split up or bundled and can be conferred to licensees with or without exclusivity.

(816) As outlined above, exclusivity is often used in association with the licensing of technology rights (limiting transmission, reception or usage technology rights, as seen in section C.3), of territorial rights (section C.4) and of release window rights (section C.5). However, one of the most important uses of exclusivity is in relation to the licensed product itself, i.e. in relation to whether or not digital content providers are entitled to offer the licensed product (content) exclusively.

(817) Both right holders and digital content providers may have incentives to contract with each other on an exclusive basis. Since users will tend to attach greater value to a provider that is in a unique position to offer a specific product, exclusivity is used by digital content providers as a means to differentiate their offerings from that of their competitors in order to compete for a wider audience. This is all the more true when the product in question is in high demand. Right holders conversely may have an interest to license their rights on an exclusive basis to extract higher revenues for their content.

- (818) The fact that exclusivity may or may not be used when licensing online rights does not necessarily imply that the offline rights are licensed on the same basis although online rights are normally licensed along with offline rights. It is possible, and indeed a widespread practice, for different transmission technology rights to be licensed on different terms as regards exclusivity.
- (819) Digital content providers have been asked to describe their licensed online rights as exclusive or not. In the analysis that follows, rights can be exclusive, non-exclusive, or mixed. The "mixed" category refers to rights that are in some cases exclusive, and in others non-exclusive, at the same time. This category covers for example instances in which the licensed right have been split by the right holder into several components and exclusivity has not been attached to all.
- (820) For example, the exclusivity might not cover all types of transmission technologies (e.g. exclusive rights may concern satellite broadcasting while online broadcasting may be non-exclusives) and / or all territories (e.g. digital content providers may be granted exclusivity only in certain Member States).
- (821) Conversely, the "exclusive" category refers to instances in which the right has been conferred in full to a digital content provider that has also been granted exclusivity, for all territories and all technologies. In light of that the "mixed" and "exclusive" categories in the figures provide an idea on the extent to which licensors have control over the licensed products – and conversely the extent to which the products to which the rights refer will not be available to other providers. Therefore, in the following paragraphs the reference to agreements with a certain degree of exclusivity will include both "exclusive" and "mixed" licensed rights.
- (822) The following figures show the overall proportions of licensing agreements containing different degrees of digital content product exclusivity across the whole EU. About half of the agreements contain some degree of exclusivity, pointing to the fact that exclusivity in different forms is widespread in the exploitation of online rights (Figure C. 58).

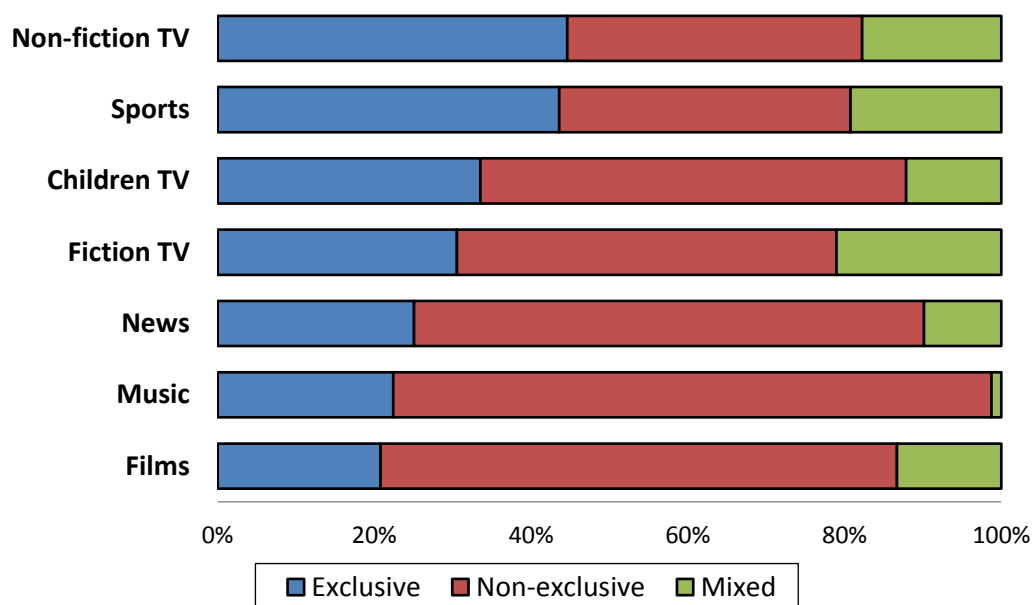
Figure C. 58: Proportion of agreements including exclusive product rights – All agreements submitted by digital content providers



(823) The pervasiveness of exclusivity is also confirmed when looking at types of content and types of service providers.

(824) With regard to the type of product, Figure C. 59 shows that exclusivity is granted in a significant proportion of agreements for all product types.

Figure C. 59: Proportion of agreements including exclusive rights – All agreements submitted by digital content providers by product type

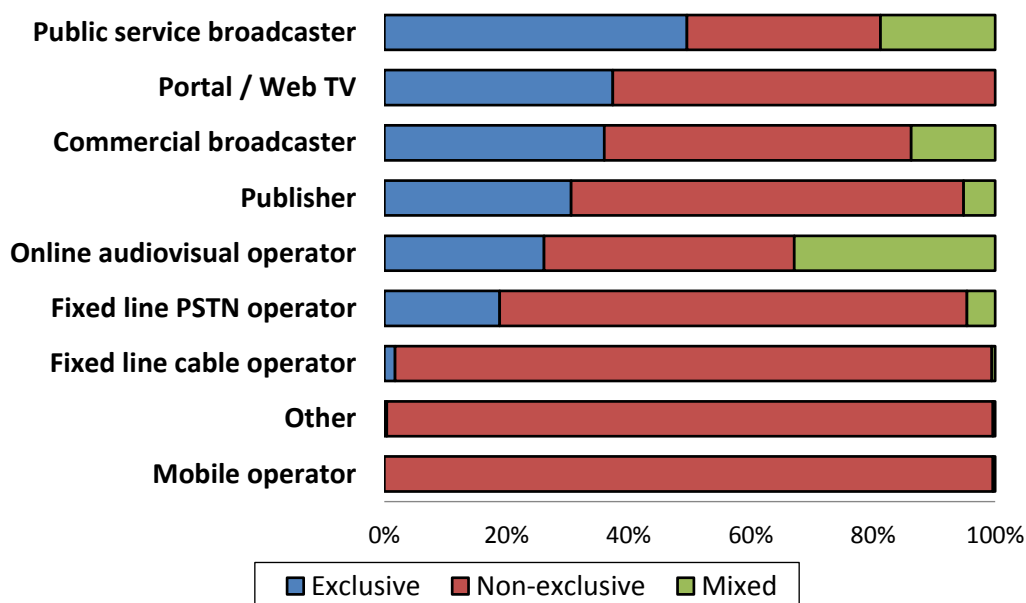


(825) The highest proportion of licensing agreements containing some degree of exclusivity is in sports and non-fiction TV agreements. The smallest proportion of exclusive

agreements can be found in music agreements, while the highest degree of exclusivity can be found in sports agreements, which normally include products considered premium content along with television fiction and so-called first-release films.

- (826) In this respect, it might seem surprising that exclusivity does not seem to be prevalent in licensing of online rights of films to a greater extent. However as the data concerns online licensing only, it is not excluded that non-online rights in films may be licensed on an exclusive basis. In addition, and more importantly, while this category includes premium content, it nonetheless contains (predominantly) library products which are of lower value and, therefore not licensed on an exclusive basis.
- (827) Exclusivity can also be analysed with regard to the type of operator (Figure C. 60) as well as by business model (Figure C. 61).
- (828) Some degree of exclusivity is found for all types of operators, with the notable exception of mobile operators and fixed line cable operators. This might indicate that electronic communications operators have more difficulty in accessing exclusive rights than other types of operators when it comes to online rights.
- (829) The opposite applies to public service and commercial broadcasters, which both have the highest proportion of agreements including some degree of exclusive rights (69 % and 50 % respectively). That can be explained by the fact that these broadcasters often simulcast on their websites content that they broadcast on-air. This content may be either externally acquired normally under exclusivity clauses or more often internally produced. In the former case, broadcasters may be exclusive licensees offline. The exclusivity which characterises the offline rights is therefore reflected in the commercial exploitation of the online rights.
- (830) A small proportion of agreements (36 %) containing some degree of exclusivity is reported by publishers (e.g. online content distributed by magazines and newspapers through their own websites). A large part of the content these operators put online is not produced by them. Such content is widely available online and therefore more widely distributed on a non-exclusive basis.
- (831) Finally more than half of the agreements of online audiovisual operators contain exclusive rights. As explained in section C.1.1.1 this category is defined broadly, including any other type of audiovisual operator only or partly offering online services. In particular, it covers different operators such as pure online distributors and operators having paid offers for which exclusivity may play an important role.

Figure C. 60: Proportion of agreements including exclusive rights – All agreements submitted by digital content providers by type of operator



(832) Figure C. 61 below, which shows the proportion of agreements containing different degrees of exclusivity by business model of respondents, seems to broadly confirm the preliminary results of the analysis discussed above with regard to types of operators. Exclusivity plays a particular role in licensing agreements of both publicly- and advertising-funded broadcasters.

(833) Operators that package own content have the highest proportion of exclusive and mixed agreements (66 %) after publicly funded operators (i.e. public service broadcasters). Packagers tend to focus their operation on packaging channels (e.g. thematic channels), which are then licensed to other operators. The content that they package can be either internally produced or externally acquired normally under exclusivity clauses (or both).

(834) Conversely, the data show that agreements submitted by hosting device operators (such as media streamers or videogame consoles) are characterised by non-exclusive online rights. The same applies to hosting online operators (for which only a small proportion of agreements is exclusive). There may however be different explanations for this result.

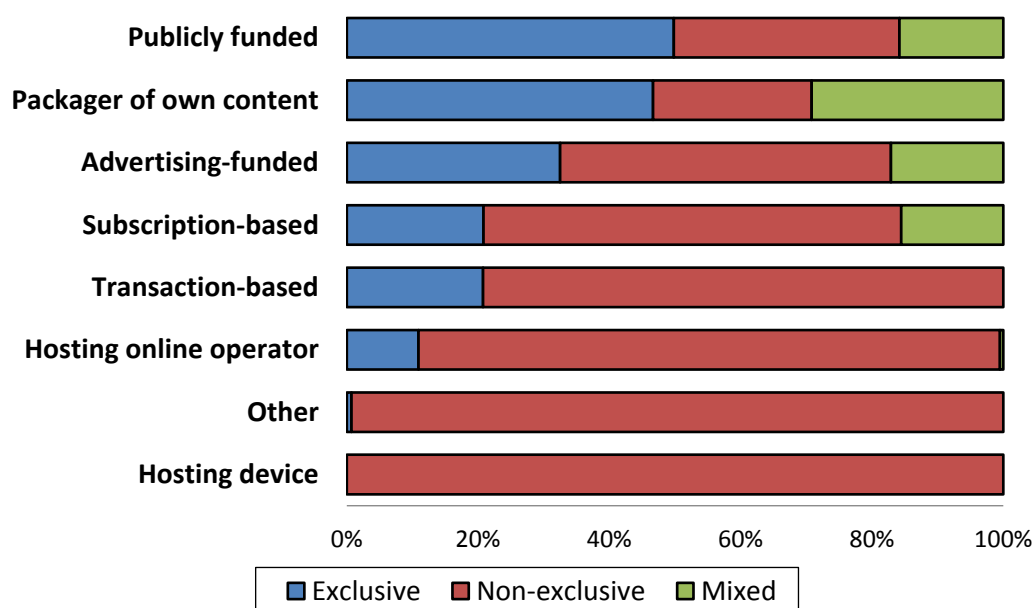
(835) For hosting device operators, online rights seem to be mainly related to on demand products. This type of offer is getting more available across different transmission technologies, and can include both products released in the first windows of exploitation (e.g. films available to rent or buy immediately after the theatrical release or TV series just released), or older products, or, at times, live events available on a pay per view basis. However the offer is strongly dependent on the availability of territorial rights, so that the range of products tends to vary substantively between Member States.

(836) Online hosting operators seem to mainly focus on library products and their offers tend not to include significant proportions of exclusive products.

(837) The preliminary results for mobile transmission rights might be seen as difficult to reconcile with section C.3.4 on technology rights exclusivity, where a significant proportion of the agreements submitted by right holders include exclusive rights to mobile transmission (Figure C. 24).

(838) The likely explanation is that whilst mobile operators may not be granted exclusive rights to mobile transmission, right holders may grant them to other digital content providers.

Figure C. 61 – Proportion of agreements including exclusive rights – All agreements submitted by digital content providers by their business model



Summary

Exclusivity is often used in association with the licensing of technology rights (limiting transmission, reception or usage technology rights) and of territorial rights. Exclusivity is also used in relation to the licensed product itself, i.e. in relation to whether or not digital content providers are entitled to offer the licensed product (content) exclusively. Exclusivity in different forms is widespread in the exploitation of online rights.

7. DURATION OF LICENSING AGREEMENTS AND CONTRACTUAL RELATIONSHIPS

(839) The duration of the licensing agreement or of the contractual relationship between a right holder and a content service provider is, together with the technological and territorial scope of the agreement or relationship a key component of licensing of rights in content.

(840) The Commission asked right holders to provide information about the duration of both agreements and contractual relationships and for information about the use of renewal clauses as well as clauses giving the contracting party the right to a first renegotiation of an agreement.

7.1 Duration of on-going licensing agreements

(841) In relation to on-going licensing agreements, right holders were asked to indicate the duration (in months) of each of the eight most valuable agreements that were submitted to the Commission in the course of the sector inquiry.

(842) Figure C. 62 below indicates that a non-negligible number, i.e. 14 %, of the submitted licensing agreements were concluded for a duration of between 5 and 10 years. Another 9 % of the submitted agreements were concluded for a time period of beyond 11 years. A few respondents have moreover indicated that their agreements were concluded for a period of 20 years or beyond.

(843) The preliminary results of the sector inquiry also show that the average duration of the licensing agreements varies depending on the digital content category concerned. As follows from Figure C. 63 below, the average duration of the submitted licensing agreements in music is shorter than the average duration of the agreements concerning rights in sports as well as fiction and children TV.

Figure C. 62: Duration of licensing agreements - Proportion of all agreements submitted by right holders

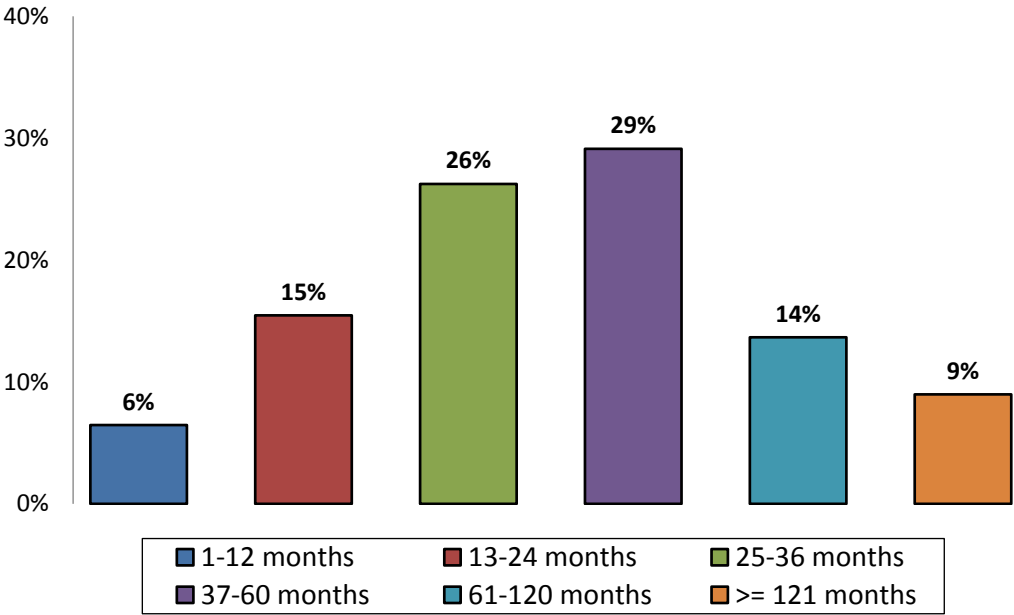
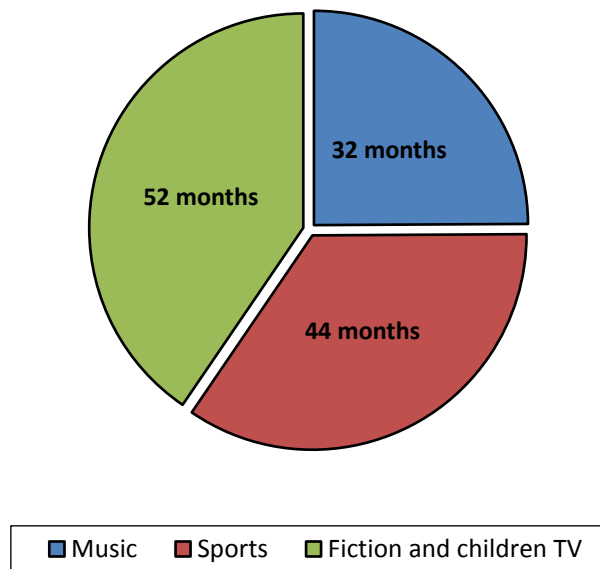


Figure C. 63: Average durations of the submitted licensing agreements - All agreements submitted by right holders - Per genre

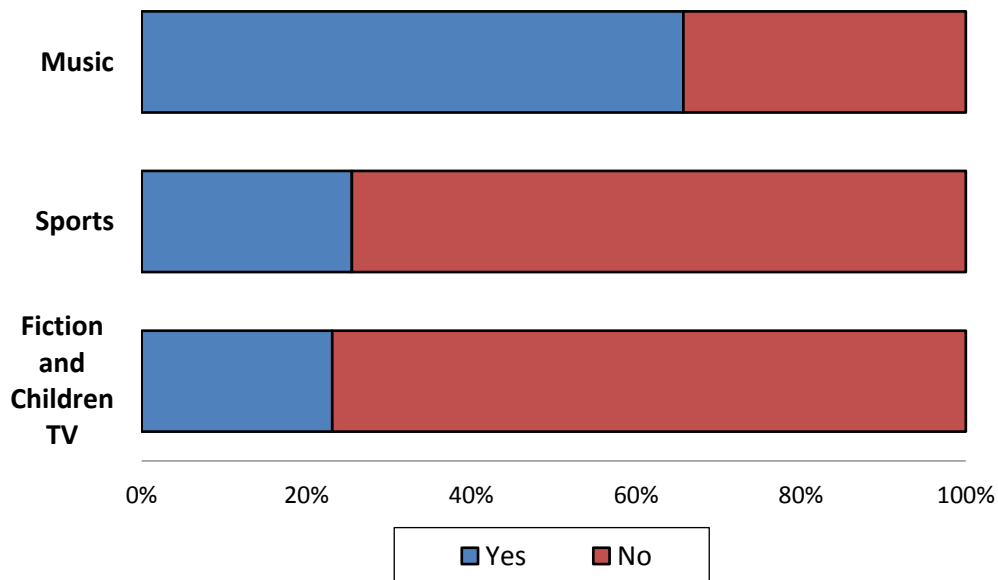


7.2 First time agreements

(844) In order to obtain information about the extent to which right holders are contracting with new contracting parties, right holders were asked whether it was the first time they had concluded a licensing agreement with a specific contracting party.

(845) Figure C. 64 below shows that the responses from music right holders indicate that a large number (66 %) of all the submitted licensing agreements were first time contracts. The number of respondents holding rights in sports content and in TV content that replied that it was the first time they had concluded a licensing agreement with their contracting party is much lower. Around 23 % of right holders in fiction and children TV content and 26 % sports right holders indicated that the submitted licensing agreements had been concluded with a new contracting party.

Figure C. 64: Proportion of first time agreements between the contracting parties – All agreements submitted by right holders – Per genre



7.3 Length of the existing contractual relationships

(846) Right holders were also asked to indicate, in relation to the licensing agreements that were not identified as first time agreements, since when they were having a contractual relationship with the specific contracting party.

(847) Figure C. 65 below shows the average length of the contractual relationship between a right holder and its contracting party. The replies submitted by right holders indicate that the average contractual relationship between right holders and their contracting parties are longer in the sports as well as fiction and children TV sectors, than in the music sector.

(848) Figure C. 65 shows that music products are to a larger extent than sports and fiction and children TV content licenced to new contractual parties with whom the right holder started a contractual relationship between 1 and 5 years ago. 42 % of the submitted licensing agreements concerning music rights were concluded with contracting parties with whom the contractual relationship started between 1 and 5 years ago. The corresponding figures for sports are 4 % and for fiction and children TV 29 %.

(849) The preliminary results of the sector inquiry also show that the contractual relationships in the sectors sports and fiction and children TV are on an average longer than in the music sector. According to Figure C. 65 below, over 70 % of all the contractual relationships in the sports and fiction and children TV sectors have lasted for at least 6 years. As regards licensing of rights in music content, it follows from the submitted data that the longest contractual relationships are between 11 and 15 years long. These correspond to 25 % of all submitted agreements from music right holders. Figure C. 65 also shows that for licensing agreements submitted by sports right holders and right

holders in fiction and children TV that 21 % of the contractual relationships in the sports sector and 21 % of the contractual relationships in fiction and children TV, have been on-going for more than 20 years ago. Some respondents indicate that they have had contractual relationships with the same provider of content for over 70 years (i.e. before the existence of digital content).

Figure C. 65: Average length of the contractual relationship - All agreements submitted by right holders - Per genre

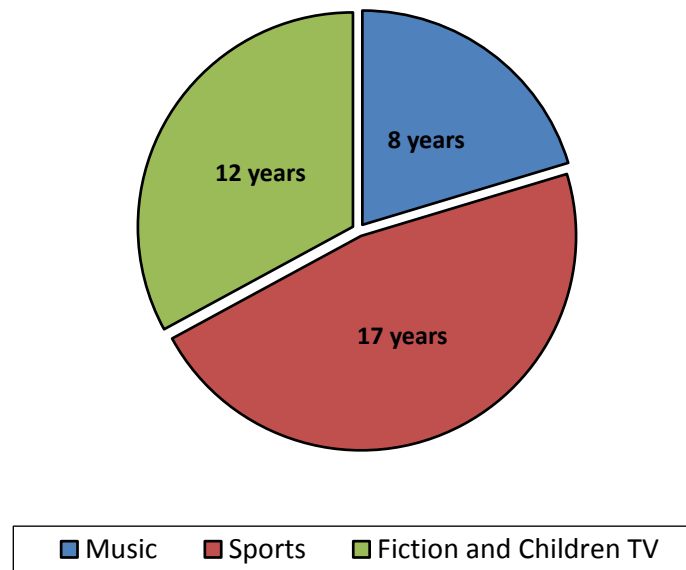
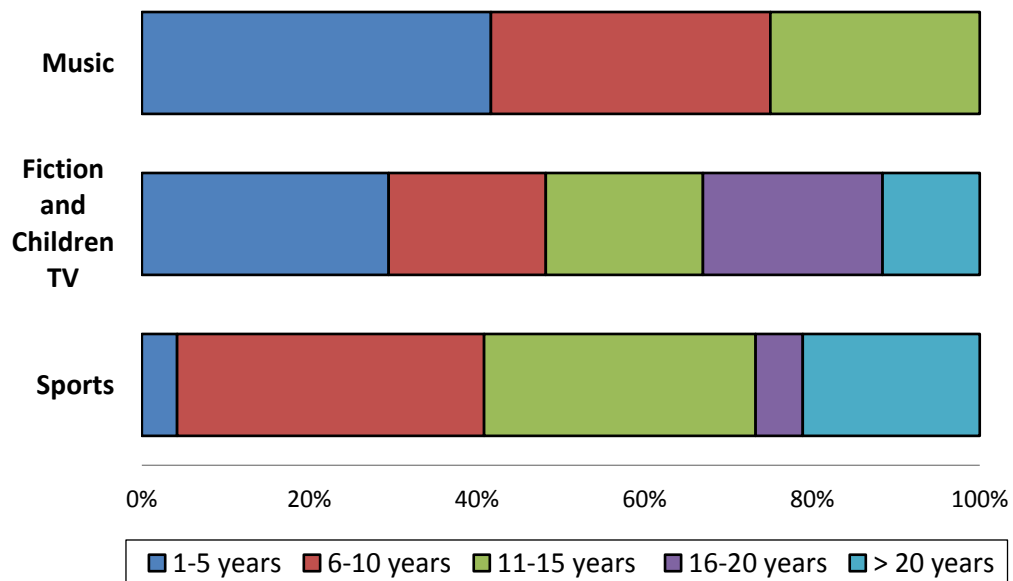


Figure C. 66: Proportion of agreements by length of the contractual relationship - All agreements submitted by right holders – Per genre



7.4 Renewal clauses and rights of first refusal

7.4.1 *Right of first refusal*

- (850) The right of first refusal is a contractual right that gives its holder the option to enter a business transaction, according to specified terms, before the other contracting party is entitled to enter into a transaction with a third party.
- (851) Where such a right exists in relation to the licensing of rights in digital content, it allows the digital content service provider to choose whether to prolong an existing contract, e.g. to obtain the rights in future episodes of the TV-series covered by existing agreements with the same right holder.
- (852) It follows from Figure C. 67 below that the almost a fifth of all the licensing agreements submitted by right holders contain the right of first refusal. According to Figure C. 67, none of the agreements regarding licensing of music rights contain the right of first refusal.³⁴⁶ The right of first refusal is rather common in agreements on fiction and children TV (27 %) and it also exists in agreements licensing sports rights but is less frequent in these types of agreements (3 %).
- (853) Some respondents which replied that their agreements do not contain any right of first refusal did however mention that their agreements do instead contain the right of first (re)negotiation. This right offers the digital content provider a possibility to negotiate exclusively with the right holder before the latter can negotiate with third parties. In contrast to the right of first refusal, the right of first negotiation does most often not provide for an option to conclude a transaction on already defined terms.

³⁴⁶ Figure C. 68 does therefore not include any results for music.

Figure C. 67: Proportion of the submitted licensing agreements that contain the right of first refusal - All agreements submitted by right holders

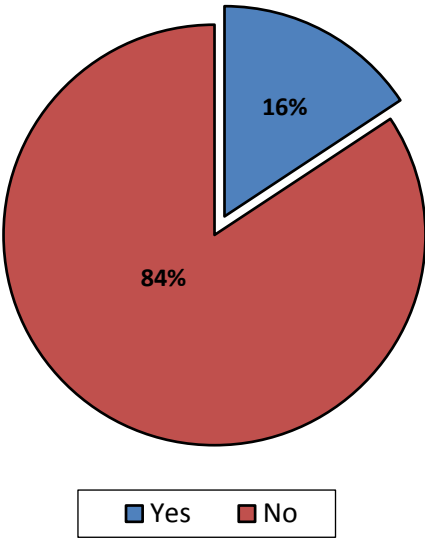
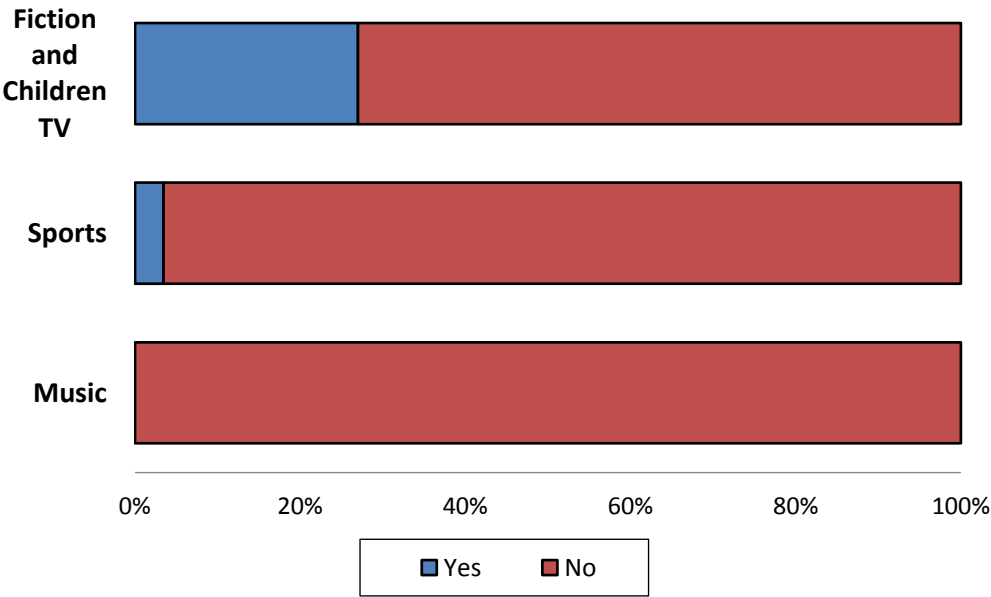
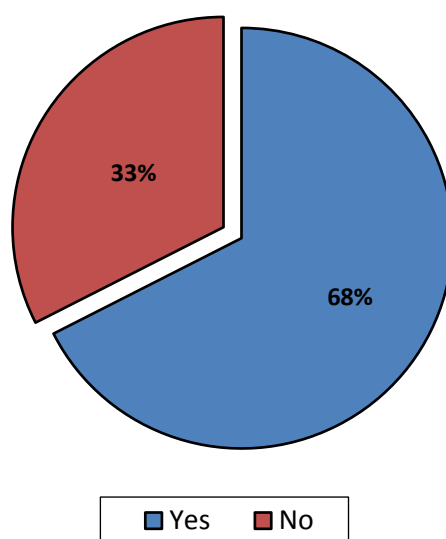


Figure C. 68: Proportion of agreements providing for a right of first refusal – All agreements submitted by right holders - Per genre



(854) Figure C. 69 below shows to what extent the right of first refusal contained in licensing agreements was actually exercised. According to Figure C. 69, the right was exercised in relation to 33 % of all the submitted licensing agreements that provide for that right. As regards licensing agreements concerning rights fiction and children TV content, the right was exercised on the basis of 65 % of the agreements that provide for such a right.

Figure C. 69: Proportion of agreements on the basis of which the right of first refusal was exercised - All agreements submitted by right holders



7.4.2 Renewal clauses

(855) An automatic renewal clause is a clause that would typically stipulate that an agreement will automatically renew at the end of each term for a further defined period unless one of the parties to the agreement gives notice of termination.

(856) Right holders were asked whether the submitted agreements had been renewed on the basis of an automatic renewal clause.

(857) According to the responses that are presented in Figure C. 70 below only a minority, 6 %, of the agreements had been renewed on the basis of such a clause. Figure C. 71 shows that it is mostly the licensing agreements submitted by music right holders (corresponding to 24 % of the submitted licensing agreements in music) that were renewed on the basis of an automatic renewal clause.

(858) Renewal clauses can relate to agreements potentially or actually including licences for a large number of products, or agreements for valuable products, or, as it often happens, a combination of the two. So-called output deals would frequently imply that a right holder licences all its rights to a digital content provider over the course of several years.

Figure C. 70: Proportion of agreements that were renewed on the basis of an automatic renewal clause – All agreements submitted by right holders

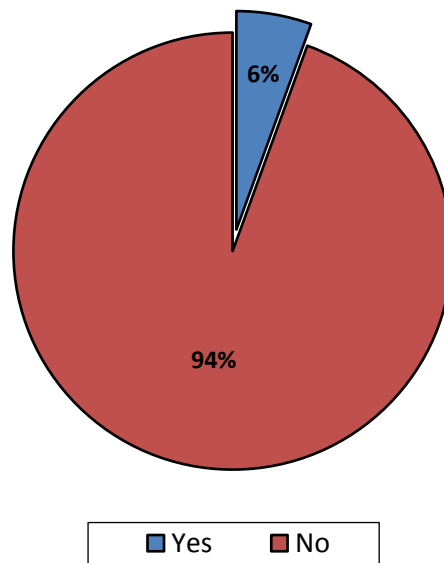
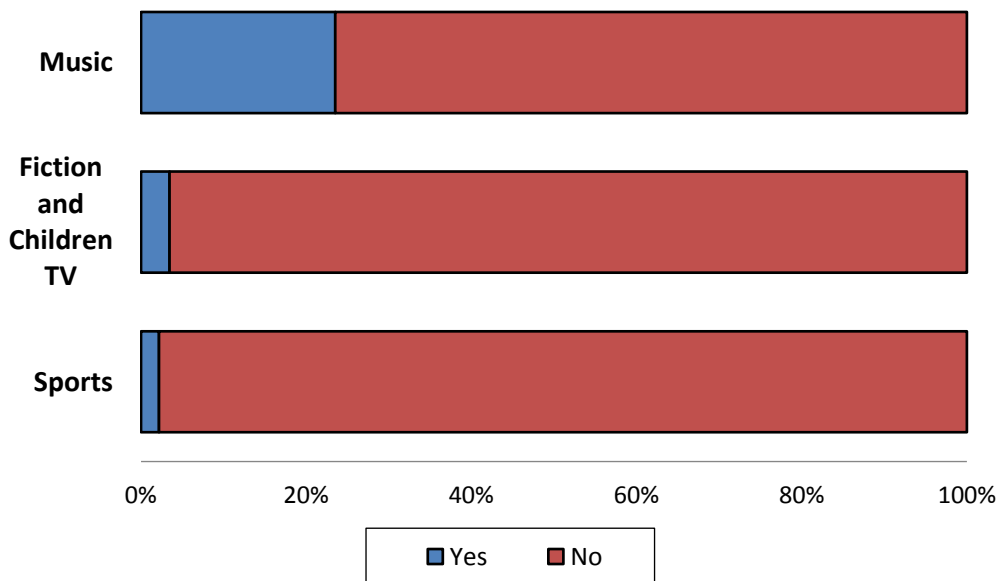


Figure C. 71: Proportion of agreements that were renewed on the basis of an automatic renewal clause – All agreements submitted by right holders – Per genre



7.5 Matching offer rights

(859) Both the licensing agreements submitted by right holders and by digital content providers sometimes contain clauses providing for a matching offer right. This right, which is often exercised when the duration of a certain agreement comes to an end, enables the digital content provider to match an offer made by a third party competitor, or make a higher offer. Where an agreement contains a matching offer right and the

right holder receives an offer from a third party for the rights covered by the right, the right holder must first inform its existing contracting party of the third party offer in order to enable the contracting party to make a matching offer which the right holder then has to accept.

(860) The scope of matching offer rights may differ from one licensing agreement to another. Such a right may apply to the rights in a certain product or in future versions of a product covered by an existing agreement or to rights in different products. The use of matching offer rights increases market transparency, since it allows the contracting party to know who its competitors are, and also price transparency, since at least the beneficiary of the right will know what his third party competitor has offered. The use of matching offer rights may constitute a way to extend the duration of an existing agreement or a contractual relationship.

Summary

Licensing agreements are often concluded for rather long durations and contracting parties often renew existing agreements. Such renewal of licensing agreements is sometimes done on the basis of specific clauses such as automatic renewal clauses and clauses providing for a right of first negotiation, a right of first refusal or a matching offer right. The fact that contracting parties often decide to contract again or renew or extend existing licensing agreements instead of contracting with new parties, leads to long term contractual relationships. This is likely to make it more difficult for new players to enter the market, or for existing operators to expand their current commercial activities into e.g. other transmission means such as online, or to other geographical markets.

8. PAYMENT STRUCTURES IN DIGITAL CONTENT LICENSING AGREEMENTS

(861) The metrics and concepts underlying the payments requested by right holders for the acquisition of the right to commercially exploit a specific product and offer it as part of a digital content service are one of the key elements in the commercial relationship between upstream suppliers/right holders and downstream digital content providers and can have substantive repercussions on how downstream markets are structured and operate.³⁴⁷

8.1 Definitions and data set

(862) This section will make use of the data set described in section C.6 in part A, i.e. a set of more than 6 800 agreements provided by both digital content providers and right holders.

³⁴⁷ This section focuses exclusively on wholesale payments by digital content providers to rights holders. Retail payments by users to digital content providers are not relevant, except where they are used as a metric in the licensing agreement (for example, when a licensing agreement refers to subscription or transaction volumes).

(863) For online rights, respondents were asked to describe what type of payments their agreements contained. In particular, each class of respondents had the possibility to choose among the categories indicated below (with multiple responses allowed):

(a) **Digital content providers:**

- Flat fee per content: A single, fixed price for a single product;
- Flat fee per package of items: A single, fixed price for a bundle of products;
- Fixed fee per download/stream: A single, fixed price per sale;
- Variable fee per download/stream: A multiple, variable price per sale;
- Fixed fee per subscriber: A single, fixed price per subscriber;
- Variable fee per subscriber: A multiple, variable price per subscriber;
- Minimum guaranteed return per content: A minimum payment to be made for each type of product, regardless of the level of sales, subscribers or other performance metrics;
- Minimum guaranteed return overall: A minimum payment to be made per bundle of products, regardless of the level of sales, subscribers or other performance metrics; and
- Other: Any other type of payment mechanism.

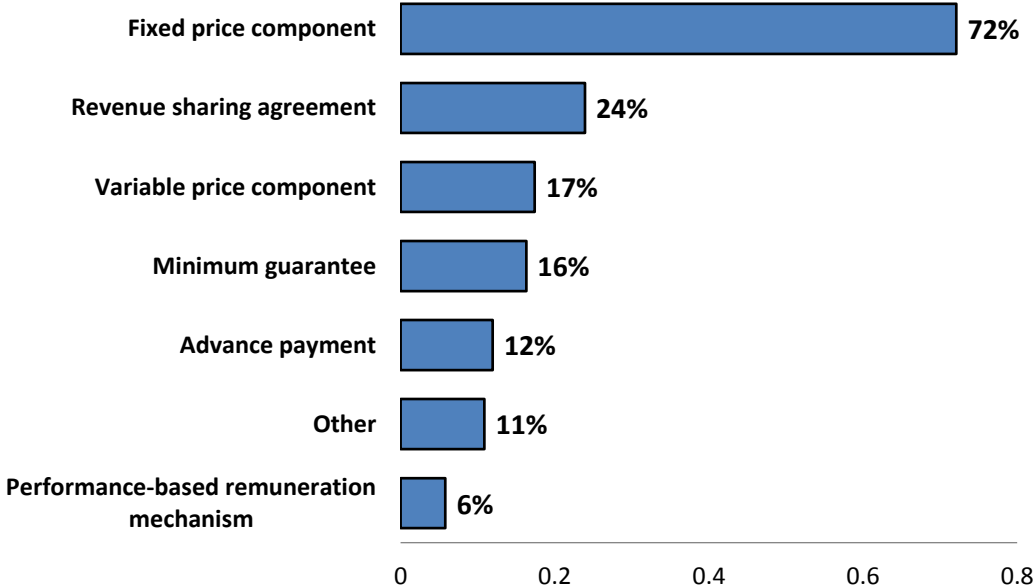
(b) **Right holders:**

- Advance payment: A payment upfront, regardless of the type of payment and independent of the buyer's performance;
- Minimum guarantee: A minimum payment to be made per bundle of products, regardless of the level of sales, subscribers or other performance metrics;
- Variable price component: A multiple, variable price element;
- Fixed price component: A single, fixed price element;
- Revenue sharing agreement: A payment proportional to the level of revenues generated by selling the specific product;
- Performance-based remuneration mechanism: A payment based on metrics linked to the sale or other type of performance of the specific product; and
- Any other: Any other type of payment mechanism.

8.2 Payment structures for online rights: Overall, by product type and by type of operator

(864) Fixed price components and revenue sharing agreements are the most recurring forms of payment for online rights sold by right holders (Figure C. 72).

Figure C. 72: Proportion of agreements including each specific payment mechanism – All agreements submitted by right holders



(865) When looking at the different types of products in the agreements submitted by digital content providers, and similarly to what was reported in Figure C. 72 in relation to technology rights, the structure of payments for television fiction and film products is the most complex.

(866) Most of the television fiction agreements (Figure C. 73) require digital content providers to pay fixed fees per bundle of products or per individual products. The typical metric used is an entire season of a TV series, or an individual episode, depending on the business model adopted by the digital content provider.

(867) Film agreements (Figure C. 74) are even more complex. A significant proportion of agreements include different types of payment for the rights needed to offer online digital content services. The most used are flat fees per film but also variable fees per download / stream and fixed fees per download / stream.

(868) Online transmissions and online business models have led to the introduction of new payment models allowing digital content providers, and ultimately users, to buy per product access to content (in terms of streams or downloads) or bundles (again in terms of streams or downloads, but often on the basis of a "light" subscription model, i.e. a subscription relationship with no fixed duration and that users can terminate and re-activate without any penalties).

Figure C. 73: Proportion of agreements including a specific payment mechanism – Fiction TV agreements submitted by digital content providers

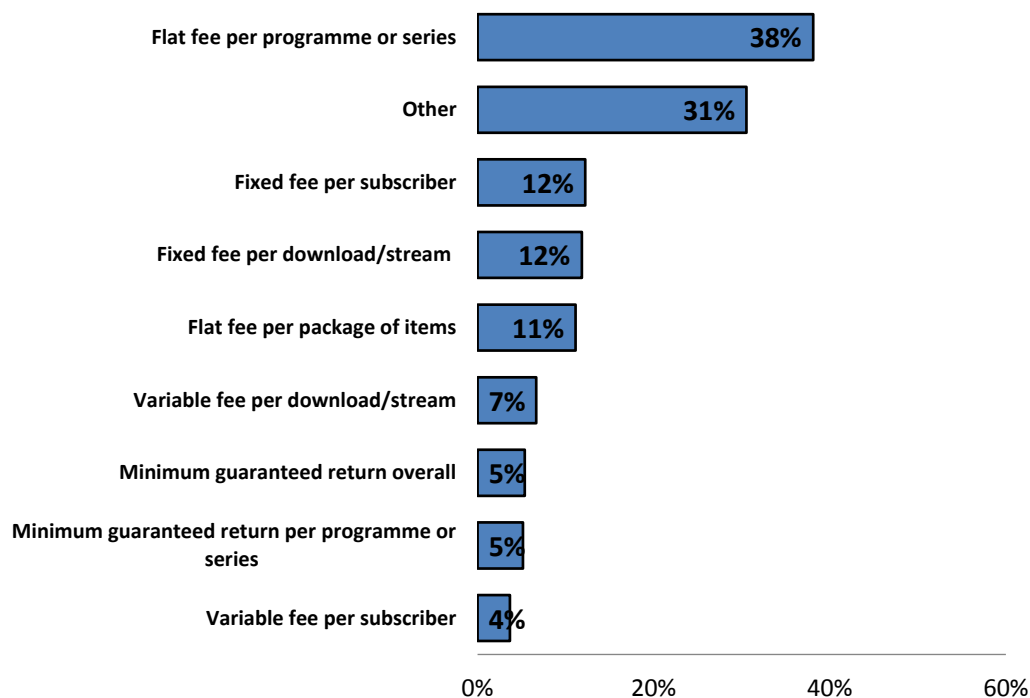
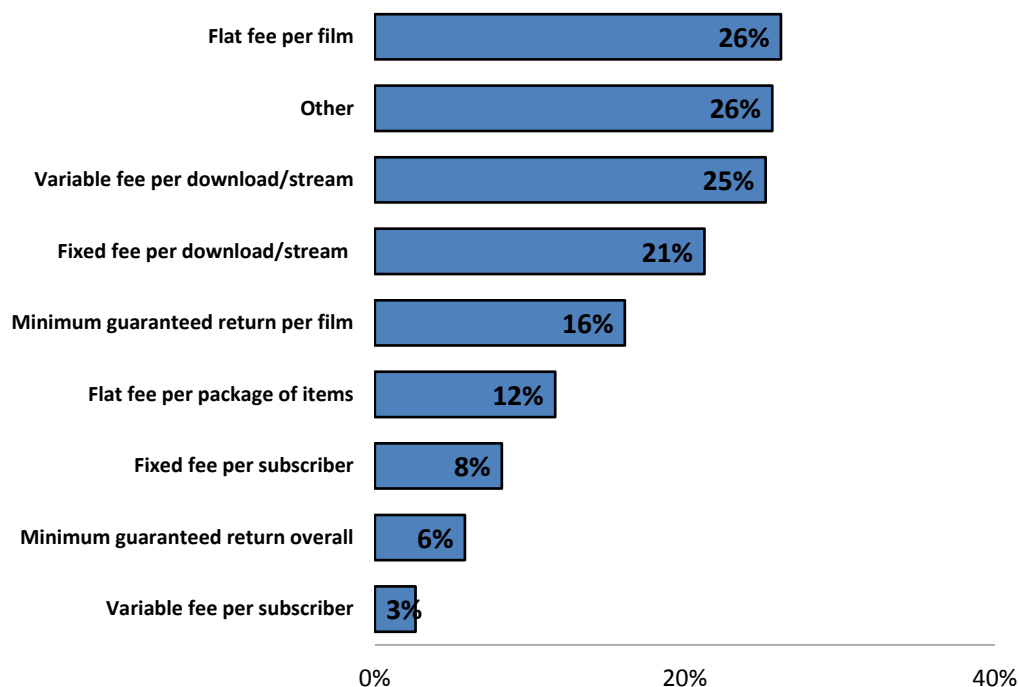


Figure C. 74: Proportion of agreements including a specific payment mechanism – Film agreements submitted by digital content providers

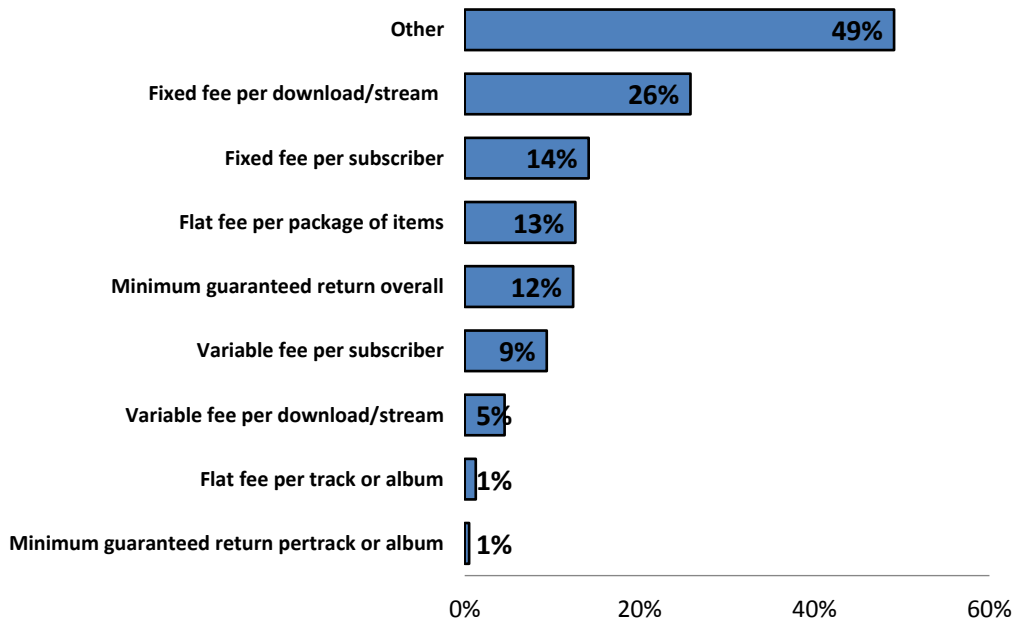


(869) A significant minority of respondents indicated that their agreements contain flat fees per packages of products – typically in the form of so-called "output deals", where a bundle of current and sometimes future products are licensed on the basis of pre-defined

payment criteria, which include, among other types of payments, a minimum guaranteed return for each product or a minimum fee for the bundle.

- (870) A large part of respondents used the "other" category to specify that online rights are sold in full or in part as a bundle with other rights. However in almost the totality of these cases it was confirmed that the payment structure for the bundle of rights includes the top categories mentioned in Figure C. 74, i.e. fixed fees or flat fees.
- (871) A large part of respondents also used the "other" category to explain how different payment mechanisms applied to different content services – for example variable fee payments per unit for downloading and a revenue share for other types of video on demand (e.g. streaming), possibly in combination with minimum guaranteed prices. Other respondents clarified that the revenue sharing agreement for their on demand service is calculated on net revenues and not on gross revenues.
- (872) A substantial minority of respondents explained that their payment structure is more complex than the categories mentioned in the questionnaires. In particular, some agreements require digital content providers to pay a figure which is the greater one between two or more figures that were the result of different calculation methods and often rely on different metrics. For example, digital content providers may be required to pay the greater between a combination of fixed fees per subscriber / per sale and a guaranteed minimum payment.
- (873) Another substantial minority pointed to the use of so-called "ladder" of payment, where fixed fees per subscriber, or per sale, change at certain thresholds, which are specified in the agreements. Normally the higher the threshold, the lower the fixed fee per subscriber or per sale but typically only in respect of the particular rung of the ladder (i.e. contributions are not lowered for the totality of subscribers / sales but only in respect of those attained in excess of the threshold).
- (874) Music agreements have the largest proportion of "other" types of payment (Figure C. 74). When looking at the explanations provided it becomes clear almost the entirety of these responses refer to the use of "greater of" formulas mentioned above.

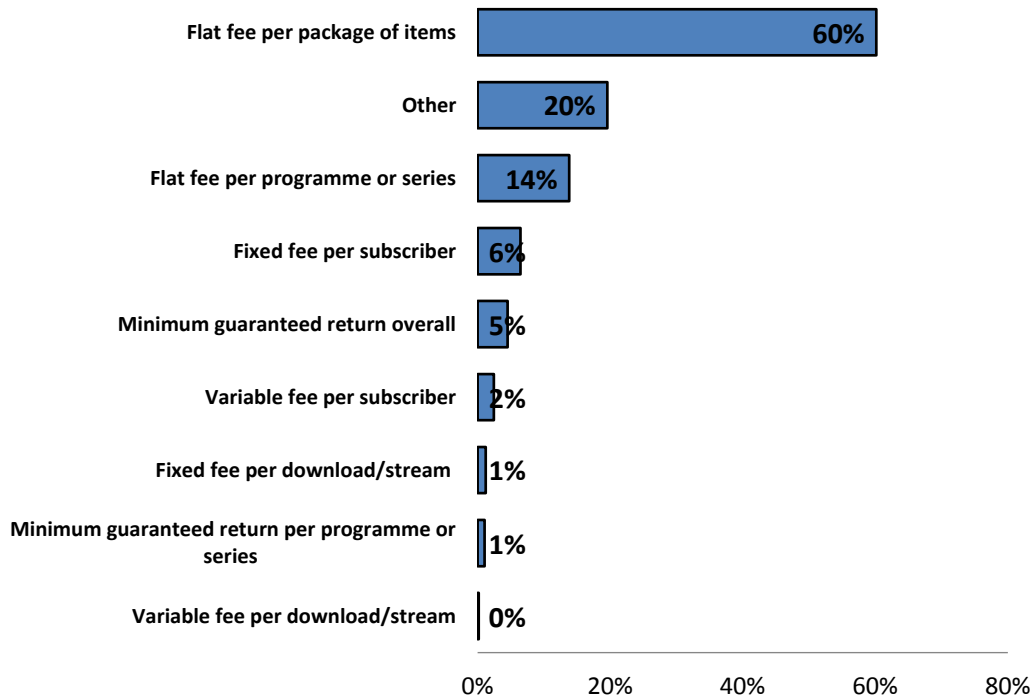
Figure C. 75: Proportion of agreements including a specific payment mechanism – Music agreements submitted by digital content providers



(875) "Greater of" formulas in music agreements may compare, for example, a pre-determined share of the revenues, a per-subscriber minimum payment, a fixed or variable rate per use (download, stream or play), and even revenue shares based on the level of market share of the digital content provider. The greater of the resulting payments will be the consideration to be paid to right holders.

(876) Finally, sports agreements have a proportionately far larger use of flat fee per package of products, typically in the form of the license to produce and distribute digital content for an entire sports event, including individual matches or other types of sub-events.

Figure C. 76: Proportion of agreements including a specific payment mechanism – Sports agreements submitted by digital content providers



(877) When looking at the types of operators, commercial and public service broadcasters are the ones whose agreements include the largest proportion of flat fees per content (Figure C. 77 and Figure C. 78 respectively).

(878) At the same time, cable and mobile operators are the ones that conclude agreements including the largest proportions of minimum guarantees, in particular both on specific products and on overall revenues (cable operators, Figure C. 79), and on overall revenues (mobile operators, Figure C. 80).

Figure C. 77: Proportion of agreements including a specific payment mechanism – Agreements submitted by commercial broadcasters

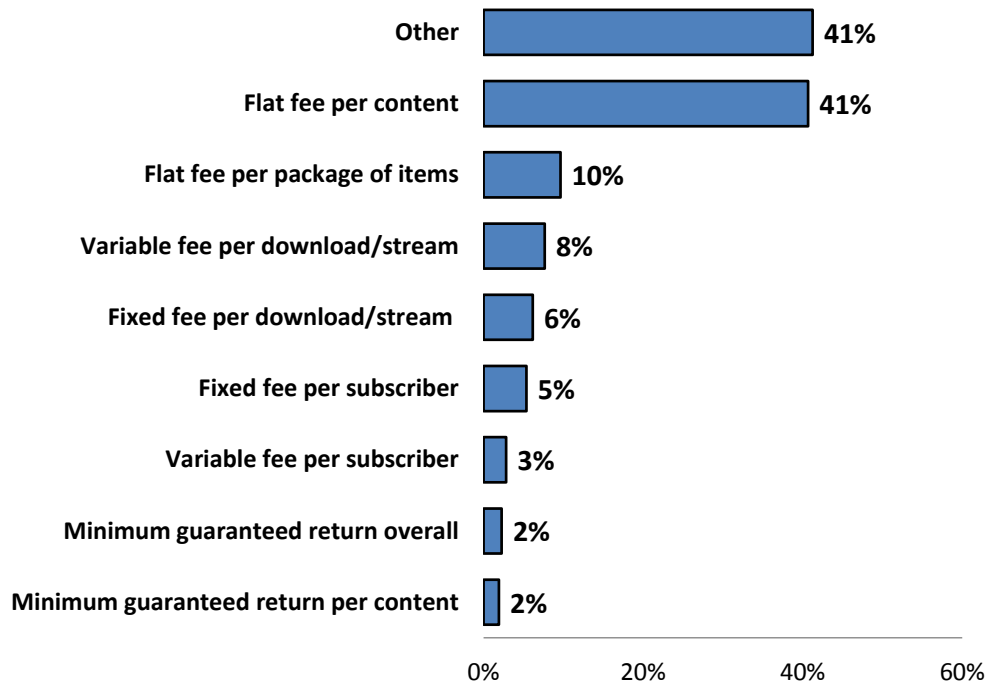


Figure C. 78: Proportion of agreements including a specific payment mechanism – Agreements submitted by public service broadcasters

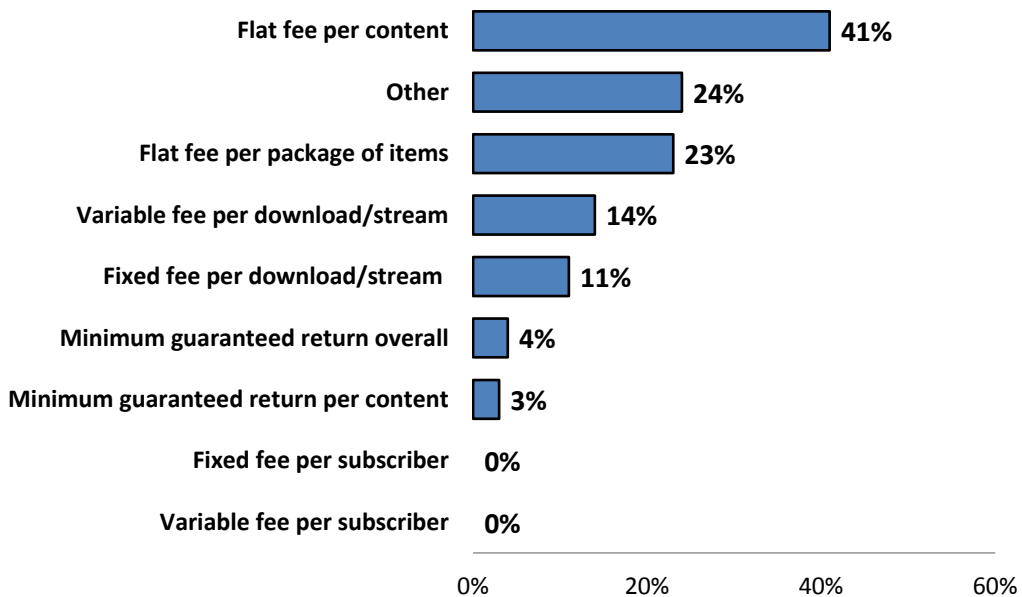


Figure C. 79: Proportion of agreements including a specific payment mechanism – Agreements submitted by cable operators

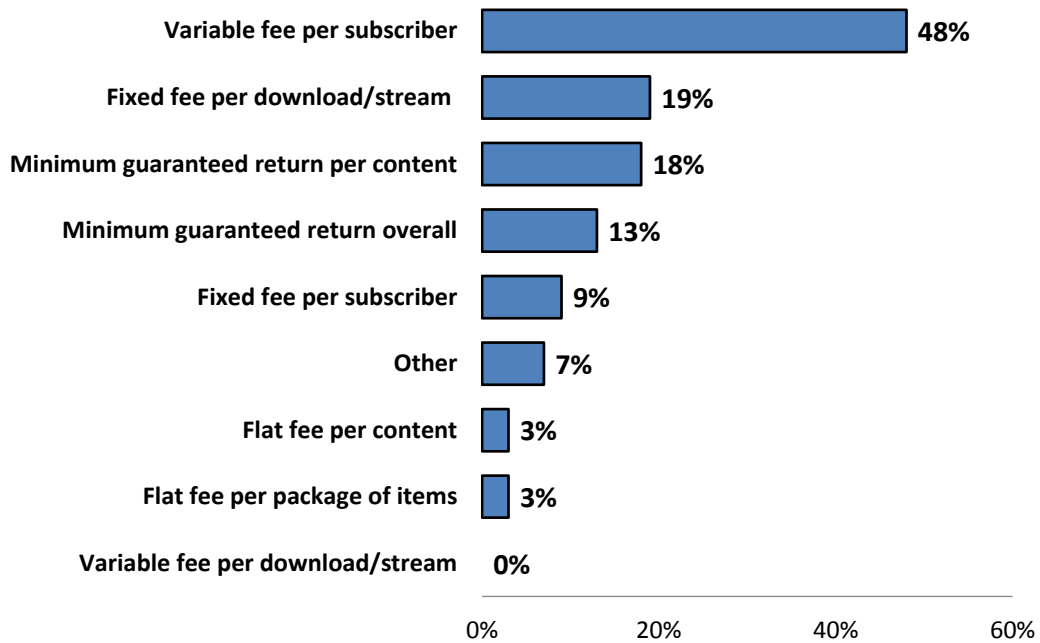
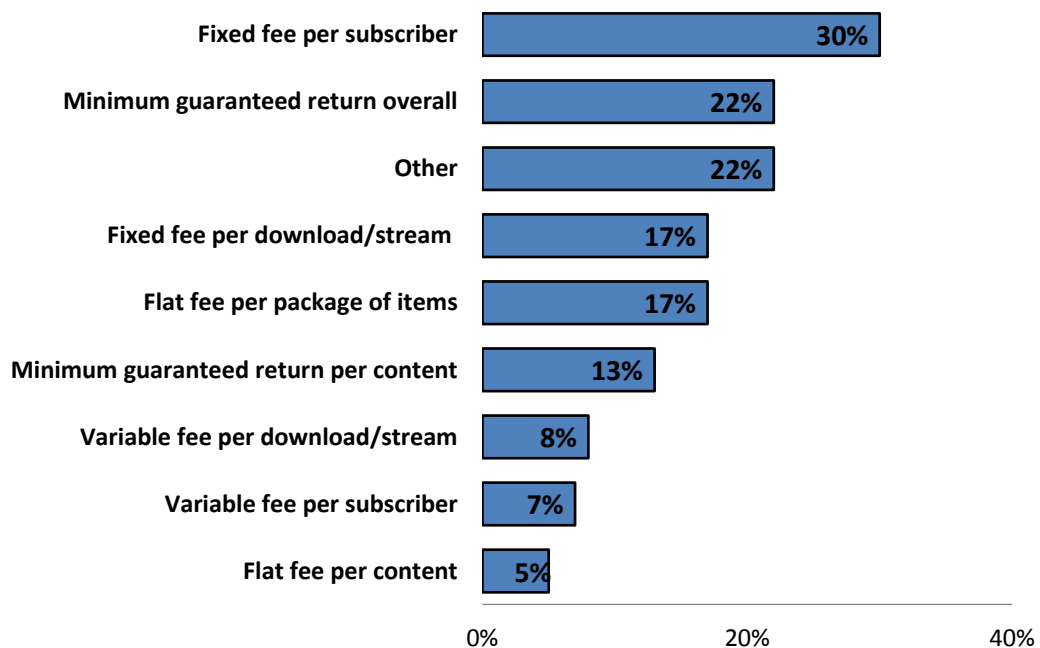


Figure C. 80: Proportion of agreements including a specific payment mechanism – Agreements submitted by mobile operators



8.3 Payment structures: combinations of specific payment mechanisms

(879) Often combinations of the payment mechanisms described in section C.8.1 above are used.

(880) In particular, advance payments are used together with fixed price components in more than one out of ten agreements. Minimum guarantees, on the other hand, are often used together with revenue sharing agreements (in slightly less than 10 % of the agreements), but also with variable and fixed price components (7 % of the agreements each). Table C. 8 shows the most frequent combinations of two separate payment mechanisms in the agreements provided by right holders.

Table C. 8: Combinations of two separate payment mechanisms in the same agreement – All agreements submitted by right holders

Combinations of specific payment mechanisms	Frequency
Advance Payment - Fixed price component	11%
Variable price component - Fixed price component	10%
Minimum guarantee - Revenue sharing agreement	9%
Variable price component - Revenue sharing agreement	8%
Minimum guarantee - Variable Price component	7%
Minimum guarantee - Fixed price component	7%

(881) The extent to which minimum guarantees are used in conjunction with other mechanisms becomes clearer when looking at combinations of three mechanisms (Table C. 9).

Table C. 9: Combinations of three separate payment mechanisms in the same agreement – All agreements submitted by right holders

Combinations of specific payment mechanisms	Frequency
Minimum guarantee - Variable price - Fixed price component	7%
Variable - Fixed price component - Performance based remuneration mechanism	7%
Minimum guarantee - Variable price - Performance based remuneration mechanism	6%
Minimum guarantee - Variable price - Revenue sharing agreement	6%
Minimum guarantee - Fixed price price - Performance based remuneration mechanism	5%
Minimum guarantee - Fixed price price - Revenue sharing agreement	5%
Minimum guarantee - Variable price - Other	4%
Variable - Fixed price component - Revenue sharing agreement	4%

(882) Less than 10 % of agreements use three payment mechanisms. Within this group of agreements combinations of minimum guarantees with variable and / or fixed prices, and with revenue sharing or performance sharing mechanisms are most prevalent.

8.4 Level of Payments

(883) In terms of the level of the payments there is a relatively high degree of variation between product types, and within each product type.

(884) Right holders were asked to provide the total amount of considerations paid for each of the agreements submitted, for the period 2011 to 2014. Table C. 10, Table C. 11 and Table C. 12 provide the results for television programmes, sports and music right holders respectively. Only agreements including, in full or in part, the licensing of online rights were included.

(885) Agreements provided by sports right holders contain the highest figures in terms of total amount of considerations paid by digital content providers. However some of the agreements provided were not with digital content providers but with specialised production houses or intermediaries, such as media rights agencies. Hence the total amounts provided might not include all payments received by sport right holders.

(886) At the opposite end, music right holders seem to typically conclude licensing agreements with lower levels of payments.

Table C. 10: Total amount of considerations paid per year – Average, minimum and maximum of the agreements submitted by television fiction and children television right holders, million EUR

Year	Average	Max	Min
2011	7.88	16.52	0.67
2012	10.42	28.09	0.54
2013	8.57	32.08	0.04
2014	6.08	36.90	0.01
2015	8.46	44.03	0.03

Table C. 11: Total amount of considerations paid per year – Average, minimum and maximum of the agreements submitted by sports right holders, million EUR

Year	Average	Max	Min
2011	22.60	66.45	0.93
2012	32.52	158.85	1.09
2013	40.57	193.65	0.39
2014	40.93	260.01	0.22
2015	31.22	207.16	0.20

Table C. 12: Total amount of considerations paid per year – Average, minimum and maximum of the agreements submitted by music right holders, million EUR

Year	Average	Max	Min
2011	0.11	0.28	0.02
2012	0.73	1.94	0.06
2013	1.60	5.20	0.05
2014	3.47	13.42	0.06
2015	6.22	22.12	0.08

Summary

The payment mechanisms which determine the amounts digital content providers have to pay right holders for the licensed online rights are highly complex. There is a variety of different payment mechanisms at play in most licensing agreements, with fixed prices, minimum guarantees and advance payments being used extensively. It seems that online transmissions and online business models have led to the introduction of new payment models allowing digital content providers, and ultimately users to buy on a per product basis for access to content (in terms of streams or downloads) or bundles of content (again in terms of streams or

downloads under subscription models for users). However, the information provided during the sector inquiry also points to the widespread use of minimum guarantees and fixed / flat fees, often in conjunction with advance payments, which might make it more difficult for new entrants to gain a foothold in the market.

9. FINANCING OF DIGITAL CONTENT PRODUCTS

- (887) Both digital content providers and right holders were asked to provide data on costs of producing digital content, as well as information linking such costs to the revenues generated through licensing. While the low response rate to the financing questions both from right holders and digital content providers makes it difficult, if not impossible, to identify a prevalent trend, the following issues can be observed.
- (888) Right holders were asked to describe their sources of financing and, particularly, to indicate, for their most valuable products the total production costs and any considerations or payments that they might have received from third parties including public funds.
- (889) In first place, many right holders indicated that they are not in the position to provide this information as they exploit the distribution rights acquired from independent production companies. With regard to sports, for instance, right holders explained that they could not provide any indication of the production costs as they do not produce the event, rather they purchase the broadcast and the related rights from a third party.
- (890) Amongst the right holders that were able to provide information, some indicated that all their production is self-financed. In a few instances self-financing is accompanied by certain production incentives, e.g., tax incentives, granted by public authorities at national/local level both outside and within the EU.
- (891) In some instances third party financing covers more than a half of the production costs, while in others only a minor portion. One right holder indicates that all production costs of a number of its products were fully covered by third parties. Regarding the type of third party funding, in one instance private equity has been indicated amongst the sources of financing. For the rest, production costs seem to be covered by digital content providers, e.g. broadcasters.
- (892) Digital content providers were asked to indicate the total amount that they have invested in co-financing or co-production of content in each of the years 2012-2014 and to explain how they take decisions regarding whether to co-finance or co-produce certain content.
- (893) The responses to these financing questions by digital content providers are few. Table C. 13 and Table C. 14 below show the average proportion of co-financing / co-production out of the total content budget by type of operator and by business model in the years 2012-2014.

(894) As shown by Table C. 13 publishers and fixed line cable operators have the highest percentages of content budget invested into co-financing/co-production, followed by public service broadcasters. This may be explained by the fact that publishers and fixed line cable operator do not have their own content and they may therefore fully rely on third party productions.

(895) Co-financing / co-production are important means to secure rights also for public service broadcasters that invest a non-negligible part of their content budget in it. This is confirmed also by the results of the analysis with regard to publicly funded operators in Table C. 14 below.

(896) In Table C. 14 below, it is interesting to note that transaction-based operators have the highest percentages of content budget invested into co-financing / co-production. This is somewhat surprising given that digital content providers using such business model normally operate on a revenue sharing basis.

Table C. 13: Average co-financing / co-production investment as a proportion of total content budget, by type of operator and by year

Type of operator	2012	2013	2014	Aggregate 2012-2014
Commercial broadcaster	6.50%	4.97%	8.33%	6.60%
Fixed line cable operator	42.24%	41.05%	38.38%	40.55%
Fixed line PSTN operator	0.31%	0.19%	0.25%	0.25%
Mobile operator	3.59%	2.25%	2.30%	2.71%
Online audiovisual operator	9.03%	9.28%	10.20%	9.50%
Other		18.45%	28.71%	23.58%
Portal / Web TV	3.36%	4.02%	3.06%	3.48%
Public service broadcaster	18.56%	22.12%	19.04%	19.90%
Publisher	100.00%	100.00%	100.00%	100.00%
Average	14.26%	15.07%	15.41%	14.91%

Table C. 14: Average co-financing / co-production investment as a proportion of total content budget, by business model and by year

Business model	2012	2013	2014	Aggregate 2012-2014
Advertising-funded	16.26%	15.94%	18.20%	16.80%
Hosting device		18.45%	28.71%	23.58%
Hosting online operator	11.04%	8.03%	3.45%	7.50%
Packager of own content	3.23%	1.22%	3.81%	2.75%
Publicly funded	15.67%	19.70%	16.22%	17.20%
Subscription-based	13.88%	13.72%	12.95%	13.51%
Transaction-based	50.45%	50.64%	50.61%	50.57%
Average	14.26%	15.07%	15.41%	14.91%

- (897) As regards the decisions whether to co-finance or co-produce certain content, digital content providers explain that this is made on a case-by-case basis taking into account different considerations including the likely return, cultural significance and creative quality.
- (898) In particular, some respondents point out that the process is not profit-driven and that the decision as to whether to co-finance / co-produce a certain production depends first and foremost on its content. In particular, co-production / co-finance allow a programme supply which is more targeted to the national audience.
- (899) In relation to the amount of money to invest in the co-production / co-financing, a key consideration is the likely return on the investment. That return depends on the rights obtained in exchange for the co-financing arrangements and is the result of the negotiations between the different parties involved. For example a respondent indicates that since the costs of entering into a co-finance or co-production arrangements is greater than acquiring third party content, it will seek to acquire exclusive rights to recoup the investment in the project. In this regard another respondent points out that co-productions are a means to obtain a larger scope of rights and exclusivity.
- (900) Some digital content providers also indicate that co-financing and co-production arrangements may also be used to ensure compliance with investment obligations or local content requirements (e.g. obligations to invest in independent production).

Summary

The low response rate to the financing questions both from right holders and digital content providers makes it difficult, if not impossible, to identify a prevalent trend. For example, many right holders indicate that they are not in the position to provide this information as they exploit the distribution rights acquired from independent production companies. In some instances third party financing covers more than a half of the production costs, while in others only a minor portion. The decision whether to co-finance or co-produce certain content is made on a case-by-case basis taking into account different considerations including the likely return, cultural significance and creative quality.

D. KEY PRELIMINARY FINDINGS

1. KEY PRELIMINARY FINDINGS: GOODS

(901) This Preliminary Report identifies the key features of e-commerce (1.1) that have a substantial effect on distribution strategies and that may give rise to potential barriers to competition (1.2).

1.1 Key features of e-commerce with a substantial effect on distribution strategies

1.1.1 Price transparency leading to an increase in price competition

(902) Online price transparency is a feature that strongly affects the behaviour of buyers and sellers. 53 % of respondent retailers track the online prices of competitors, and 67 % also use automatic software programmes for that purpose. 78 % of those retailers that use software to track prices subsequently adjust their own prices based on those of their competitors.

(903) While price is a key parameter of competition for retailers, product quality and brand image are key for manufacturers. Increased price competition at the retail level results in manufacturers adopting a variety of business strategies in order to better control the distribution quality and the image and positioning of their brands.

1.1.2 Free-riding

(904) Customers can switch swiftly between online and offline sales channels. Many customers use the pre-sales services offered by one sales channel (such as product demonstration, personal advice in a brick and mortar shop or search for product information online) but then purchase the product on the other sales channel. In such cases the costs of pre-sales services become difficult to recoup ("free-riding").

(905) Creating a level-playing field between offline and online distribution channels and finding a solution to free-riding, thereby preserving the investments in high-level pre-sale services is a consideration that is claimed by stakeholders to play an important role in generating some of the observed market trends and restrictions.

1.1.3 Increased direct retail activities by manufacturers

(906) With a view to both reaping the benefits of online sales and better controlling distribution, many manufacturers have opened their own online shops in the last 10 years. The product category with the highest proportion of vertically integrated manufacturers and retailers is cosmetics and healthcare. As a result, in the last decade, many retailers have found themselves competing against their own suppliers.

1.1.4 Expansion of selective distribution

(907) In the last 10 years, as a reaction to the growth of e-commerce, 19 % of respondent manufacturers introduced selective distribution systems for the first time and 67 % of the respondent manufacturers that already used selective distribution introduced new

selection criteria. These criteria seek to a large extent, both in relation to online and offline sales, to ensure high quality distribution, coherent brand image and the quality of pre- and after-sales services.

(908) The use of certain clauses in selective distribution agreements may go beyond what is necessary to achieve the goals of selective distribution. For example, the requirement for retailers to operate at least one brick and mortar shop (thereby excluding all pure online players from selective distribution), while generally covered by the Vertical Block Exemption Regulation, may need further assessment in individual cases (where necessary, via the withdrawal of the benefit of the Vertical Block Exemption Regulation) when used for certain product categories or certain lines of products which online retailers might be equally qualified to sell.

(909) As a follow-up to the sector inquiry, it may become necessary for the Commission to scrutinise certain clauses restricting online sales (specifically those mentioned in the following chapters), in particular in selective distribution agreements, more closely.

1.2 Potential barriers to competition

1.2.1 Cross-border sales restrictions

(910) The preliminary findings show that 38 % of the retailers use geo-blocking in order to restrict cross-border online sales. While most of the geo-blocking measures are based on the unilateral decision of retailers, nearly 12 % of retailers report that they have contractual cross-border sales restrictions in at least one of their product categories. The product category in which the highest proportion of retailers experience cross-border sales restrictions is clothing and shoes, followed by consumer electronics.

(911) Contractual cross-border sales restrictions have multiple forms and are not always written in agreements, but may also be communicated orally.

1.2.2 Restrictions on the use of marketplaces

(912) 20 % of the manufacturers report that they sell products directly to buyers via marketplaces. 14 % started to do so in the last 10 years as a reaction to the growth of e-commerce.

(913) The importance of marketplaces as a sales channel varies significantly depending on the size of the retailers, the Member States as well as the product categories: 61 % of the respondent retailers do not use marketplaces for their sales, and only 4 % responded that they were selling solely via marketplaces. Marketplaces are more important as a sales channel for smaller and medium-sized retailers with a turnover below EUR 2 million while they are of lesser importance for larger retailers with a higher turnover. The importance of marketplaces as an online sales channel differs significantly from one Member State to another with a high proportion of retailers using marketplaces in Germany (62 %) and the United Kingdom (43 %) compared to substantially smaller proportion in Austria (13 %), Italy (13 %) or Belgium (4 %). In terms of product

categories, marketplaces are most relevant for retailers selling clothing and shoes and consumer electronics.

- (914) 18 % of retailers report to have marketplace restrictions in their agreements with their suppliers. The prevalence of marketplace restrictions varies a lot between Member States. The Member States with the highest proportion of retailers having marketplace restrictions in their distribution agreements are Germany (32 %) and France (21 %). Marketplace restrictions encountered in the sector inquiry range from absolute bans to restrictions on selling on marketplaces that do not fulfil certain quality criteria.
- (915) The preliminary findings do not show that marketplace bans would generally amount to a de facto prohibition to sell online. The importance of marketplaces differs significantly between Member States, product categories and size of retailers concerned. Overall, the retailers' own online shops remain an important online sales channel and more than half of the respondent retailers sell via their own online shop only. The differences between Member States, product categories and sizes of retailers confirm that the potential impact of marketplace restrictions on competition needs to be assessed on a case-by-case basis.

1.2.3 Restrictions on the use of price comparison tools

- (916) The preliminary findings of the sector inquiry indicate that the use of price comparison tools is widespread with 36 % of retailers reporting that they supply data feeds to price comparison tool providers in 2014. While certain manufacturers consider price comparison tools as beneficial for their business, increasing their brand's visibility, a substantial number of them see price comparison tools rather critically as they further enhance competition on price, rather than on other features.
- (917) 9 % of retailers report that they have agreements with manufacturers which contain some form of restriction in their ability to use price comparison tools. The proportion of retailers affected by price comparison tool restrictions is highest in Germany (14 %), Austria (13 %) and the Netherlands (13 %). The price comparison tool restrictions encountered in the sector inquiry range from absolute bans to restrictions based on certain quality criteria.
- (918) Absolute price comparison tool restrictions, i.e. restrictions which are not linked to quality criteria may exclude an effective method for retailers to generate traffic to their website.

1.2.4 Pricing restrictions

- (919) Resale price maintenance is one of the practices manufacturers and retailers may make use of in response to the increased online price competition and, in particular, to the high online price transparency and low search costs for customers, allowing them to swiftly compare prices.

- (920) By observing a minimum retail price, both manufacturers and retailers may minimise the impact of quick online price erosion, thereby protecting both the level of the wholesale price the manufacturers can ask for the product, and the profit margins retailers can expect.
- (921) At least a third of the retailers in each product category covered by the sector inquiry reports to receive some form of price recommendations from manufacturers. Nearly 30 % of manufacturers indicate that they systematically track the prices of their products sold via independent retailers. Others do so in a targeted manner (on certain products, key markets). 67 % of the respondent manufacturers use manual tracking, while nearly 40 % make (also) use of price-tracking software to track prices. Almost a third of respondent retailers report that they normally comply with the price indications given by the manufacturers while slightly more than a quarter say that they do not comply.
- (922) Increased price transparency through price monitoring software may facilitate or strengthen collusion between retailers and thereby impact competition.
- (923) While manufacturers often voice their intention to create a level-playing field between online and offline sales channels, taking into consideration potential differences in cost levels, dual pricing (setting different wholesale prices depending on the sales channel) is rarely considered as a viable option due to the risk that a dual pricing strategy could be in breach of Article 101(1) TFEU.

2. KEY PRELIMINARY FINDINGS: DIGITAL CONTENT

2.1 Licensing of rights: A key factor for competition in online digital content services

- (924) Securing attractive digital content is essential for digital content providers that wish to maintain or improve their competitive position, as emphasized by virtually all respondents. While online transmission offers the possibility to innovate the provision of access to products and services, demand for digital content services is ultimately driven by demand for the content offered. From this perspective, the main driver of competition remains the same: attractive content.
- (925) Digital content providers effectively translate users' demand for certain services into a wholesale demand for the rights that enable them to make the content available to users.
- (926) The terms on which rights are made available to digital content providers are therefore one of the most important drivers of competition. However, online distribution of content and demand for online rights does not seem to have altered the way in which right holders license their rights.
- (927) Right holders often split up their rights in several components and monetise each of them separately, with a view to maximising their value over the entire life cycle of the content.

(928) The following specific issues in relation to the licensing of rights in digital content emerge from the responses to the sector inquiry.

2.2 Contractual restrictions in relation to transmission technologies, timing of releases and territories

(929) Rights can be and are licensed using any type of combination along technologies, release windows and territories. Moreover, exclusivity can be attached to all, none or only parts of the licensed rights.

(930) The licensing agreements between right holders and digital content providers therefore define the main parameters of competition as regard the online distribution of digital content.

(931) The preliminary results of the sector inquiry show that contractual restrictions, in terms of licensed transmission technologies, timing of releases and licensed territories, are the norm in digital content markets.

(932) In order to offer online services, digital content providers need to secure licences to a minimum set of rights to market the content. This set of rights typically includes the right to transmit online via digital technology; the right to allow users to access the content via a receiving device; and the right to use certain technologies to deliver the content, such as streaming.

(933) Whether such online rights are available depends on several factors, including the specific content, its commercial history, the specific release window sought, and the specific territory where the digital content provider wishes to operate.

(934) This means that it may be difficult for new entrants to secure licenses to provide digital content online, regardless of whether they already provide other content (offline) or are active in other geographic markets, with the notable exception of music content.³⁴⁸

(935) As regards territorial contractual restrictions, in addition to the fact that rights are often licensed on a national basis, the preliminary results of the sector inquiry show that a large majority of digital content providers are required by rights holders to restrict access to their online digital content services for users from other Member States by means of geo-blocking. Moreover, many of these agreements contain clauses enabling the right holder to monitor the implementation of technical geo-blocking measures, suspend distribution, or as a final resort, terminate the licensing agreement or ask for compensation, where the measures are not implemented and used in accordance with the rights holders' requirements.

³⁴⁸ This concern seems to apply less to music products than all other products on which the sector inquiry sought evidence. This is due to the fact that music products tend to be licensed with fewer restrictions and make less use of exclusive licensing.

2.3 Duration of the agreements

- (936) New entrants and smaller operators wishing to grow their digital content businesses may find it difficult to obtain licenses also because of the relatively long and stable exclusive contractual relationships between right holders and established digital content providers.
- (937) Right holders tend to have relatively long-term agreements with digital content providers. Digital content providers seeking to enter a certain market or expand their existing commercial activities in a market may therefore face difficulties in accessing rights that are the object of long-term exclusive licensing agreements between their competitors and right holders.
- (938) This may be exacerbated by certain contractual clauses that are part of the licensing agreements, such as first negotiation clauses, automatic renewal clauses and other similar clauses. Explicit or implicit (re)negotiation clauses may affect the possibilities of possible new entrants and smaller operators wishing to grow their online digital content businesses.

2.4 Payment structures

- (939) The widespread use of advance payments, minimum guarantees and fixed / flat fees (per bundle of programmes, or independently of the number of programmes) implies that smaller digital content providers or new entrants may have to pay the same amount as larger incumbents for the equivalent rights, and often they may have to do so upfront.
- (940) Without the possibility of making their financial contributions to right holders dependent on their size, their user base or the number of products they distribute, new entrants and smaller operators may be at a disadvantage compared to established digital content providers when attempting to secure attractive rights for digital content. For example, a new entrant wishing to adopt an innovative business model might not be in a position to make a competitive bid for the rights, if faced with widespread licensing practices requiring the use of payment mechanisms that might not suit their chosen business model.
- (941) However, the variety of payment mechanisms found in the agreements submitted also suggests that some degree of experimentation takes place. For example, for some types of products and release windows (e.g. films, television fiction and non-fiction offered on demand in the earliest windows), revenue sharing and performance-based payment mechanisms (e.g. where payments are proportionate to the number of subscribers or users accessing the content) seem to be more widely used than alternatives. A range of digital content providers, such as hosting devices providers, hosting online services providers, online audiovisual operators or fixed line operators, appear to be in a position to offer exactly the same content (e.g. the same films or television fiction or television non-fiction products) for rent or for sale, in streaming or download modalities.
- (942) Such arrangements, where several digital content providers are able to acquire the rights to the same content on a non-exclusive basis, favour competition downstream, increase

choice for users, and make use of the possibilities offered by online transmission. However, such arrangements seem to be used only in a handful of Member States.

(943) The use of certain payment methods such as minimum guarantees and advance payments can in certain situations allow right holders to share risks more efficiently for products that may have, on an individual basis, a high risk profile, given their uncertain prospects of success at the time of the investment.³⁴⁹

2.5 Impact of licensing practices

(944) The availability of the relevant rights for online distribution of digital content is one of the key determinants of competition among digital content providers. There are a number of important factors that determine the availability of rights, such as the (technological, temporal and territorial) scope of rights as defined in the licencing agreements between right holders and digital content providers, the duration of the licencing agreements and the widespread presence of exclusivity.

(945) The preliminary results of the sector inquiry raise the question whether certain licensing practices may make it more difficult for new online business models and services to emerge and for new or smaller players to enter existing markets or to grow and expand their activities into other markets. This may be particularly true when online rights are sold exclusively on a per Member State basis or bundled with rights for other transmission technologies.

(946) Some respondents, for example some fixed and mobile electronic communications operators, voiced concerns in this respect, suggesting that the impact of some or all of the licensing practices described above hamper their ability to obtain licenses, and as a consequence limit their possibility to compete in providing online digital content services.

(947) Some respondents identify in particular the way online rights in digital content are split up or bundled, the prevailing payment mechanisms, and the stability of existing commercial relationships between right holders and incumbent content providers, including provisions such as matching or automatic renewal clauses, as key factors that, when combined, ultimately put them at a competitive disadvantage. Other respondents indicate that current licensing practices, in particular the fact that rights are often licensed on an exclusive basis, effectively allow only large-scale incumbents to act as the only distributors, in particular allowing them to secure the most attractive content. They also claim that opportunities for new entrants exist only in fringe or niche markets, i.e. in relation to products that are widely available on a non-exclusive basis, such as library products.

³⁴⁹ Little substantive evidence was provided on the importance of pre-sale arrangements to fund new products by respondents, in relation to the products included in the sector inquiry.

- (948) Regarding exclusive licencing, the preliminary results of the sector inquiry point to complex licencing practices, whereby exclusivity may be granted in different forms (such as in relation to territory, technology and time), as well as complex payment mechanisms. It also emerges clearly that certain types of (attractive) content are crucial for the ability of digital content providers to attract users and become or remain competitive.
- (949) An important element of the assessment of exclusive licensing is the presence of market power at different levels of the supply chain which, being closely related to the specific product and / or geographic market, needs to be examined on a case-by-case basis. The preliminary results of the sector inquiry also offer insights on other aspects of licencing of digital content that are relevant for the assessment of possible foreclosure of digital content providers, such as the scope and duration of licensing agreements, as well the structure of payments.
- (950) The availability of online rights depends on whether and how the rights have been split up by right holders, the extent to which they may have been bundled with other rights, and on the duration of both specific licensing agreements and contractual relationships, which in general tend to be long-term. Moreover, the choice of fee structure may in some cases increase the fixed cost of entry for digital content providers. However, the structure of payments and their level may serve other purposes, such as optimal risk sharing and streamlining of incentives along the supply chain.
- (951) At the same time, the information provided during the sector inquiry also shows that multiple business models and a great diversity of licensing practices are available and indeed used, which can cater for the needs of both right holders and digital content providers.
- (952) The Commission will therefore assess on a case-by-case basis, having regard to the characteristics of the specific product and geographic markets, whether certain licensing practices may restrict competition and whether enforcement is necessary in order to ensure effective competition.

E. LAUNCH OF THE PUBLIC CONSULTATION

- (953) With the publication of this Preliminary Report, the Commission wishes to trigger a facts-based exchange of views with stakeholders. For this purpose, DG Competition is soliciting the views and comments of interested stakeholders about the preliminary findings of the sector inquiry presented in this Preliminary Report. All stakeholders are invited to submit their comments on this report not later than 18 November 2016. All comments should be sent to the following e-mail address: COMP-E-COMMERCE@ec.europa.eu.
- (954) Respondents are advised that their contributions may be published on the Commission's website, unless the submission contains business secrets or other confidential information. Please indicate in your submission whether you consider it to contain business secrets or other confidential information. If so, please provide together with the submission a non-confidential summary of the information concerned.
- (955) The Final Report on the sector inquiry is expected to be published in the first quarter of 2017.