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The European Commission fines a clothing company for restricting online sales to its authorised retailers

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On 17 December 2018, the European Commission issued a decision in which it fined Guess EUR 39,821,000 for restricting advertising and online sales of its products to its authorised retailers in the European Economic Area (Case AT.40428 –Guess– the “**Decision**”).

This is the first decision by the European Commission in relation to the lawfulness of online sales restrictions that suppliers can impose on their distributors within a selective distribution system, with the aim of protecting their brand image, since the prominent *Coty* judgment handed down by the Court of Justice of the European Union (“**CJEU**”) on 6 December 2017 (a link to our newsletter on this topic can be found [here](#)).

► [Case AT.40428 - Guess](#)

## THE DECISION

Guess established a qualitative selective distribution system which included both monobrand and multibrand stores in several Member States. Guess also sold products directly through its own stores.

In relation to online sales, Guess imposed a series of restrictions on the sale of its products by its authorised retailers with the aim of protecting the prestige of its image and enhancing brand reputation.

The Decision considered that the following practices, conducted within a selective distribution system, were a single and continuous infringement of Article 101 of the Treaty on the Functioning of the European Union (“**TFEU**”). The Decision also clarified that the distribution agreements could not benefit from the exemption established in Regulation 330/2010 inasmuch as the agreements contained several of the hardcore restrictions laid down in Article 4 of the Regulation, notably, the prohibition to restrict passive sales and to fix prices, which prevent the whole agreement from benefitting of the exemption.

## PROHIBITION AGAINST THE USE OF GUESS’ BRANDS IN ONLINE SEARCH ADVERTISING

The Decision deemed proved that Guess systematically prevented its independent authorised distributors from using its brands for the purpose of online search advertising. In particular, it noted that Guess did not authorise them to bid for the use of its brands as search terms in Google AdWords.

The CJEU had stated in *Coty* that, within a selective distribution system, a restriction would not fall under the scope of the prohibition of Article 101(1) of the TFEU if its purpose was legitimate, it was

imposed uniformly upon all distributors, it was applied in a non-discriminatory manner and it did not exceed what was strictly necessary.

In this respect, the Decision reiterated that the CJEU acknowledged that the use of brands in online search engines could be restricted in cases in which there is a risk of confusion by the consumer regarding the origin of the products. However, the European Commission clarified that with regard to authorised retailers there is no risk of confusion regarding the legitimate origin of the products sold. Therefore, the restriction of online search advertising cannot be considered to pursue a legitimate purpose such as the protection of brand image.

The Decision focused particularly on the fact that Guess' internal documents proved that the purpose of the restriction was to prevent the increase in advertising costs regarding online search advertisements for its own brands. Guess also intended to maximise its own website's traffic at the expense of that of its authorised retailers. Given these facts, the Commission held that this limitation was a restriction of competition by object.

## **RESTRICTION TO ONLINE SALES**

The selective distribution policy applied established that authorised retailers could only sell their products online with Guess' prior written authorisation.

The investigation conducted by the European Commission showed that, unlike in physical stores, for which there were predetermined quality criteria and an authorisation procedure for authorised retailers, in relation to online distribution, Guess did not have a list of quality requirements to grant the authorisation or an authorisation procedure in place. Hence, the granting or refusal of the authorisation was discretionary.

In addition, the internal documents showed that the purpose of this restriction was to limit the number of independent authorised retailers that completed online sales as much as possible, so as to favour Guess' online sales through its own website. In fact, most of the requests for authorisation were denied.

In these circumstances, the Decision considered that the prior authorisation requirement, which was not linked to any specific quality requirement, did not comply with the requirement of uniform and non-discriminatory application stipulated by the CJEU in *Coty* and that it constituted a restriction by object.

These practices protected Guess' own online business from intrabrand competition by its authorised retailers.

### **RESTRICTION OF CROSS-SELLING AMONG AUTHORISED DISTRIBUTORS**

Guess' distribution agreements included several restrictions that limited the possibility of cross-selling among authorised wholesalers and network retailers. Notably, the agreements included clauses that limited the territory in which the distributors could sell, usually limiting them to a Member State. They also included obligations to purchase the products exclusively from Guess and the prohibition to sell to other authorised distributors.

The European Commission held that these sales restrictions between authorised wholesalers and retailers within a selective distribution network are a restriction by object and thus contrary to Article 101(1) TFEU.

### **PROHIBITION TO SELL TO CONSUMERS LOCATED OUTSIDE THE ASSIGNED TERRITORIES**

The contracts with authorised retailers established that sales rights and advertisement for products was limited exclusively to the territory of the Member State assigned. Both active sales (at the distributors' initiative) and passive sales (at a consumer's request) were prohibited. The European Commission considered this to be a restriction to competition by object, since it is capable of contributing to the partitioning of national markets and prevents the establishment of a single market. In addition, it stated that these practices are a breach of Regulation 2019/302 on geo-blocking, applicable since 3 December 2018 (a link to our newsletter on this topic can be found [here](#)).

### **FIXING THE RESALE PRICE**

The general sales conditions applied by Guess in most of the Member States established an obligation by the authorised distributors to respect recommended retail prices. Non-compliance with this obligation could result in Guess ceasing supply. The European Commission's investigation showed that Guess monitored the retail prices applied by its distributors and tried to correct any deviations detected. In practice, the prices applied in Eastern European countries were 5-10% higher than in the other European Union countries. This price-fixing constitutes a restriction by object.

## **SIGNIFICANT FINE REDUCTION FOR COOPERATING**

The European Commission reduced the fine by 50% because Guess cooperated throughout the procedure and acknowledged that the facts occurred. The possibility of granting a significant fine reduction to companies that acknowledge their involvement in the unlawful events and cooperate with the European Commission within a settlement procedure is common in cartel cases. However, the European Commission has recently decided to extend this benefit to other disciplinary proceedings such as abuses of dominant position and vertical restrictions.

The settlement procedure requires that companies acknowledge their involvement in the prohibited practices and their responsibility in them. This is the third decision that grants a significant fine reduction within a settlement procedure.

In this case, Guess not only acknowledged the facts but also disclosed information about new practices not yet known to the European Commission. Thus it provided valuable evidence in respect to the information which the European Commission already had. This was the reason why the fine was reduced significantly.

## **CONSEQUENCES AND IMPLICATIONS FOR OTHER COMPANIES**

The European Commission and national competition authorities have shown a growing interest in analysing whether distribution systems applied by companies are compatible with competition rules, notably, with respect to the application of selective distribution systems and the possible limitation of online sales.

To this end, there is still uncertainty as to how far a supplier can legitimately go in restricting online sales within a selective distribution system and, under which circumstances protecting brand image is considered a legitimate aim to justify such a restriction.

This Decision clarifies the European Commission's position in relation to some of these restrictions. In particular, the European Commission attaches great importance to establishing objective and uniform criteria to be applied in a non-discriminatory manner to all the members of the authorised distribution network.

However, based on the particular characteristics of this case, in which it was proven that the supplier's main objective was to limit its authorised distributors' online sales to benefit its own stores, the

European Commission considered some of them to be restrictions by object. In this respect, the fact that the Decision was adopted within a settlement procedure has limited the legal debate about the lawfulness of some of the sanctioned practices, which had not been examined before by the competition authorities, such as the restriction of the use of brands in online search advertising. Uncertainty remains as to whether the Commission's decision would have been different had the supplier's main objective for imposing the restriction been different.

## Contact Lawyers

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