

## RECENT DEVELOPMENT

### EEC — ARTICLE 85 — SELECTIVE DISTRIBUTORSHIP AGREEMENTS MAY NOT INCLUDE PROHIBITION ON EXPORTS

In 1975, price controls imposed by the Belgian government froze retail prices for new cars in Belgium. Consequently, BMW prices were lower in Belgium than in other Common Market countries. This price differential led to the re-export of BMW automobiles from Belgium to other countries in the Community; thus, automobiles which were manufactured in West Germany were exported to Belgium, then re-exported elsewhere.<sup>1</sup> Selling BMW vehicles to consumers by these re-export channels particularly disturbed BMW Munich, the parent company. It responded to the situation by writing to its subsidiary, BMW Belgium, concerning the detrimental effects of these re-exports of BMW vehicles into Germany. BMW Munich suggested that dealers should verify that export sales were only to approved BMW dealers in accordance with the BMW Belgium selective distribution agreement pending exemption by the Commission pursuant to Article 85(3). However, BMW Munich emphasized that "re-exports in themselves do not constitute a breach, and no objection should be taken to individual cases."<sup>2</sup>

In July 1975, BMW Belgium sent a circular to its dealers indicating its knowledge that dealers had been selling cars in the Netherlands and Germany. The circular stated that "at a time when we are having to ration car supplies we can see no justification for such sales."<sup>3</sup> In September 1975, BMW Belgium sent another circular to its dealers<sup>4</sup> which was accompanied by a cir-

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<sup>1</sup> The re-exports were accomplished in the following manners: (1) buyers in other Community countries purchased vehicles directly from Belgian BMW dealers; (2) intermediaries, not appointed by the manufacturer, handled such imports; (3) dealers which were not members of the BMW network bought cars from authorized Belgian dealers for resale to the consumer; or (4) Belgian BMW dealers sold BMW vehicles to approved dealers in Germany. Local dealers were upset by the situation as they were required to provide guarantee service on vehicles they had not sold. *BMW Belgium N.V. and Belgian BMW Dealers*, O.J. 1978, No. L 46, 33 at 34.

<sup>2</sup> *Id.*

<sup>3</sup> *Id.* at 35.

<sup>4</sup> *Id.* The circular of September, 1975, stated:

Henceforth, no BMW dealer in Belgium will sell cars outside Belgium or to firms who propose to export them. Our solidarity and the protection of our network are at stake. This absolute solidarity of the BMW network and strict compliance with

cular from the Belgian BMW Dealers' Advisory Committee.<sup>5</sup> Both circulars advocated an export ban. Forty-eight of the ninety Belgium BMW dealers indicated their support. Upon notification of the contents of the circulars, BMW Munich expressed its satisfaction to BMW Belgium. BMW Munich, however, requested BMW Belgium to bear in mind that "no action may be taken against your dealers simply because they have re-exported cars."<sup>6</sup>

Two independent German dealers, purporting to act as agents for authorized BMW dealers, found it difficult to obtain new BMW vehicles. BMW Belgium refused to supply these dealers since it believed that at least one of them was acting on its own behalf and not as an agent.<sup>7</sup> Heuer and MGH, the German dealers, thought otherwise and informed the Commission on October 20 and again on November 19, 1975, that Belgian dealers were no longer willing to supply them with new BMW models for re-export. The Commission began its investigation and, in the meantime, MGH initiated separate actions against BMW Belgium in the Belgian and German Courts.<sup>8</sup> On February 20, 1976, BMW Belgium sent a new circular to its dealers which stated that the earlier circulars were merely recommendations and were not to be regarded as instructions on exports.<sup>9</sup> The Commission held that the agreements entered into by BMW Belgium, the Belgian dealers, and the eight members of the Dealers' Advisory Committee infringed Article 85(1) of the Rome Treaty.<sup>10</sup> BMW Belgium and the Belgian dealers appealed to the Court of Justice. *Held*, affirmed. These export

this sales policy should be convincing and will help to restore confidence in the Belgian BMW network.

<sup>5</sup> *Id.* at 36. The Belgian BMW Dealers' Advisory Committee circular advised "no more sales outside Belgium."

<sup>6</sup> *Id.* at 37. The letter went on to state that "warnings may be given only where a dealer is suspected of selling cars to non-approved dealers in breach of this agreement, no action may be threatened against your dealers unless made necessary by a proved breach of their agreement."

<sup>7</sup> *Id.*

<sup>8</sup> In the Belgian Court, an amicable settlement was reached on March 11, 1976, which reflected BMW Belgium's decision to refrain from refusing to sell or allowing to be sold new vehicles to MGH through the Belgian distribution system. The agreement was on the condition that MGH limit itself to the role of an agent. MGH's action in the German court was dismissed. As to Heuer, BMW Belgium sent a letter to Heuer in January 1976, which stated that "we will not raise any objection in the future to your activity as agent."

<sup>9</sup> *Id.* at 38. In an attempt to rectify its mistake, BMW Belgium stated:

It was not in the past, nor is it now, our intention or that of the Dealers' Advisory Committee to impose specific instructions on you to prohibit you from exporting. You are to regard our circular of 29 September 1975 as null and void to the extent that it might be construed as an export prohibition.

<sup>10</sup> *Id.* at 41.

prohibitions were contrary to a fundamental principle of Community law, and the fines imposed by the Commission were upheld in full.<sup>11</sup> *BMW Belgium N.V. and Belgian BMW Dealers*, O.J. 1978, No. L 46, 33.

Article 85(1) of the Rome Treaty prohibits agreements between undertakings and concerted practices which may affect trade between Member States and which have as their objective the prevention, restriction or distortion of competition. However, Article 85(3) provides that paragraph one may be declared inapplicable if the agreement meets certain criteria.<sup>12</sup> A general principle of Community law is that an exclusive distribution agreement falls within the prohibition of Article 85(1).<sup>13</sup> Either such agreements prevent traders from making use of alternative sources of supply, or they prevent suppliers from making use of alternative distributorship agreements.<sup>14</sup> Certain of these distributorship agreements,

<sup>11</sup> The Court joined cases 32/78 and 36 to 82/78.

<sup>12</sup> Treaty Establishing the European Economic Community, March 25, 1957, No. 4300, 298 U.N.T.S. 3. Article 85 provides:

1. The following shall be prohibited as incompatible with the Common Market: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the Common Market, and in particular those which:

- (a) directly or indirectly fix purchase or selling prices or any other trading conditions;
- (b) limit or control production, markets, technical development, or investment;
- (c) share markets or sources of supply;
- (d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
- (e) make the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

2. Any agreements or decisions prohibited pursuant to this article shall be automatically void.

3. The provisions of paragraph (1) may, however, be declared inapplicable in the case of:

- any agreement or category of agreements between undertakings;
- any decision or category of decisions by associations of undertakings;
- any concerted practice or category of concerted practices;

which contributes to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit, and which does not:

- (a) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives;
- (b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.

<sup>13</sup> C. BELLAMY & G. CHILD, *COMMON MARKET LAW OF COMPETITION* 213 (2d ed. 1978).

<sup>14</sup> *Id.* at 205.

however, may be exempted *en bloc* under Article 85(3) from the prohibition contained in Article 85(1) pursuant to Regulation No. 67/67.<sup>15</sup>

One type of exclusive dealing arrangement, the selective distributorship, limits the sale of products at the distribution stage to selectively authorized dealers. Thus, dealers outside the network cannot deal in the products in question.<sup>16</sup> Frequently, suppliers wish to make use of selective criteria when choosing outlets for their products. Certain qualitative and quantitative factors may be utilized in order to insure that products are handled only by dealers who meet certain technical requirements or achieve minimum turnover. Qualitative criteria include minimum training requirements for personnel, maintenance of sufficient stocks, and the provision for after sales service. Quantitative criteria serve to limit the number of outlets in any area.<sup>17</sup> Such selective distributorships may infringe Article 85(1) and usually do not fall within Regulation 67/67.<sup>18</sup> In such cases, an individual exemption may be sought by means of notification of the agreement.<sup>19</sup> The Commission alone has the power to grant such individual exemptions as well as the power to issue regulations exempting certain categories of agreements. Regulation 67/67, which exempted certain sale distribution agreements, was adopted by the Commission as an exercise of this power.<sup>20</sup>

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<sup>15</sup> Dam, *Exclusive Distributorships in the United States and the European Economic Community*, 16 ANTITRUST BULLETIN 116, 126 (1971). Regulation 67/67 exempts until December 31, 1982, agreements and concerted practices pursuant to which the supplier agrees to sell only to the distributor for resale within a defined area of the Common Market, or the distributor agrees to buy only from the supplier, or both.

<sup>16</sup> E.E.C. COMMISSION, THIRD REPORT ON COMPETITION POLICY 20 (1974). See also Hahn, *Exclusive Distributorship Agreements In the European Common Market: Antitrust Laws on the Move*, 16 AM. UNIV. L. REV. 367 (1973). Hahn advances two arguments in support of the selective distributorship system: (1) expert handling will allow better marketing and post sales service; and (2) improved distribution of goods will permit the lowering of prices to the consumer.

<sup>17</sup> LEADING CASES AND MATERIALS ON THE COMPETITION LAW OF THE E.E.C. 271 (D. Gijlstra & D. Murphy eds. 1976).

<sup>18</sup> BELLAMY, *supra* note 12, at 227.

<sup>19</sup> W. ALEXANDER, THE E.E.C. RULES OF COMPETITION 74 (1973).

<sup>20</sup> *Id.* at 15. Thus, the parties to an agreement may seek negative clearance, a declaration that the agreement does not infringe Article 85(1) pursuant to Regulation 17 which requires notification of the agreement, or the parties may seek a declaration that the conditions of Article 85(3) are met and, consequently, the prohibition of Article 85(1) does not apply. The latter approach was taken by the Commission in the *Omega* decision, J.O. 1970, NO. L 242, 22; [1970] C.M.L.R. D 49. In an attempt to develop the foreign sales of its watches, Omega organized a distribution network comprised of exclusive importers, general agents, and a limited number of retailers. The limitation on the number of retail outlets imposed by Omega's main distributors, general agents, was by reference to potential demand, not by

Selective systems of distribution have come under the scrutiny of the Commission and the Court of Justice. Generally, restrictions which provide for the selection of dealers based on qualitative criteria necessary to insure that the goods are sold in a satisfactory manner are allowed.<sup>21</sup> However, any distributorship agreement which prohibits exports to other Member States strikes at the essence of the Common Market and will not be permitted.<sup>22</sup> The Commission decisions in *Kodak*,<sup>23</sup> *BMW Munich*,<sup>24</sup> and *Junghans*<sup>25</sup> emphasize that in order to insure the free movement of goods between the Member States, products must be able to be

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qualification. Although Regulation 67/67 did not apply, the Commission held that an exemption could be granted to the Omega agreement pursuant to Article 85(3). The Commission determined that the system of general agents improved distribution and passed on to consumers a fair share of the resulting benefit. Where products are expensive and of a high quality, it is necessary to limit outlets in order to ensure a sufficient turnover to justify the retailer's stocking a full range of products and providing service.

<sup>21</sup> BELLAMY, *supra* note 13, at 239.

<sup>22</sup> J. CUNNINGHAM, THE COMPETITION LAW OF THE E.E.C. 103 (Supp. 1973).

<sup>23</sup> *Kodak*, J.O. 1970, No. L 147, 24; [1970] C.M.L.R. D 19. Kodak had imposed export restraints on its subsidiaries by forcing purchasers of Kodak products to buy through the subsidiaries in their respective Member States. If the purchaser went outside his Member State to purchase Kodak products, the sale was invoiced through the subsidiary in his Member State at its price, thus preventing customers from shopping for better terms. The Commission held that these conditions restricted competition within the Common Market and adversely affected trade within the Community, since the end result was the isolation of each Member State's market and the protection of prices charged on each of the markets from competition from one or more Member States.

<sup>24</sup> *BMW Munich*, O.J. 1975, No. L 29, 1; [1975] 1 C.M.L.R. D 44. BMW operated a distribution system in Germany consisting of main dealers and retailers. Both groups accepted obligations set out in standard form agreements prescribed by BMW, including an obligation not to supply BMW products, except certain spare parts, to dealers not authorized by BMW. BMW selected their dealers on the basis of several objective criteria, including the quality of the dealer's premises, trained staff, and after sales service. In addition, there was a quantitative criterion to be determined on the basis of BMW's view of the needs of the market. Originally, the agreements also prohibited BMW dealers in Germany from delivering new BMW vehicles to countries other than their own. Although recognizing the restrictive effect on competition of the BMW criteria, the Commission exempted from Article 85(1) the agreements of BMW for distribution of its products in Germany upon receipt of proof that BMW had abandoned export prohibitions that would have applied in the Common Market. The Commission acknowledged that "such a system may contribute both to improving the production and distribution of goods and to promoting technical progress." BMW dealers were free to obtain supplies of BMW products from approved dealers in other Member States with whom they had no contractual relationships. Although BMW dealers are not to establish branches outside their own territories, they are not prevented from advertising or canvassing for business outside their respective territories.

<sup>25</sup> *Junghans*, O.J. 1977, No. L 30, 10. *Junghans* involved the distribution of German manufactured clocks and watches through wholesalers and retailers in Germany and through sole distributors and retailers in the other Member States. Junghans prohibited distributors in most Member States from directly or indirectly exporting to other E.E.C. countries. The Commission insisted that these restrictions be eliminated.

exported or resold for export within the E.E.C. at prices freely determined by the parties involved.<sup>26</sup>

The Commission refused to exempt the distribution agreements in the above cases until the agreements were amended to allow exports to other Member States. Additionally, the Court of Justice in *Miller v. Commission*<sup>27</sup> upheld the decision of the Commission that export prohibitions in Miller's exclusive dealing agreement constituted infringements of Article 85(1). Miller contended that because of its weak position on the market, the export prohibition could not possibly affect Community trade.<sup>28</sup> The Court held that the Commission was justified in finding that there was a danger that trade between Member States would be affected appreciably. In regard to the gravity of the infringement, the Court stated that "clauses prohibiting exports constitute a form of restriction on competition which by its very nature jeopardize trade between Member States."<sup>29</sup>

The Commission and Court of Justice decisions in *Belgium N. V. and Belgian BMW Dealers* further illustrate the Community's refusal to accept export prohibitions. The Commission imposed substantial fines on BMW Belgium and forty-eight BMW dealers which agreed to operate an export ban on new BMW vehicles.<sup>30</sup>

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<sup>26</sup> EEC COMMISSION, FIRST REPORT ON COMPETITION POLICY 61 (1972).

<sup>27</sup> *Miller v. Commission*, [1978] E.C.R. 131 (Case 19/77), [1978] 2 C.M.L.R. 334. Miller produces records, tapes, and cassettes which are distributed under the Europa and Sonic labels. In order to distribute in Alsace-Lorraine, Miller concluded an exclusive dealing agreement with Sopholest in Strasbourg. The agreement contained a clause which prohibited export of Miller products from Alsace-Lorraine to other countries. Miller also imposed export prohibitions on domestic and foreign customers.

<sup>28</sup> *Id.* at 151. The Court stated:

[I]n prohibiting agreements which may affect trade between Member States and which have as their object or effect the restriction of competition, Article 85(1) of the Treaty does not require proof that such agreements have in fact appreciably affected such trade, which would moreover be difficult in the majority of cases to establish for legal purposes, but merely requires that it be established that such agreements are capable of having that effect.

<sup>29</sup> *Id.* at 152.

<sup>30</sup> See Seventh Report on Competition Policy, April 1978, at 102-03. One circumstance in which the Commission is entitled to impose fines is where undertakings intentionally or negligently act in violation of Article 85(1). In determining what fines to impose, the Commission took into consideration the gravity of the offense, the short duration, and the part played by each party. The Commission determined that the offense was serious because it compounded restrictions already inherent in a selective distribution system by adding an export prohibition. The Commission held that BMW Munich had made BMW Belgium aware of the fact that it was acting in breach of Article 85(1) and imposed the heaviest fine on BMW Belgium as the instigator of the restrictive scheme. A lesser fine was imposed on the Advisory Committee due to its reliance on BMW Belgium. In reference to both of these groups, the Commission considered the fact that the agreement lasted only a short time; ac-

The export prohibition was not actually within the Belgian BMW distribution agreement but was called for in a BMW circular and in a circular issued by the Belgian BMW Dealers' Advisory Committee.<sup>31</sup> BMW Belgium had notified the Commission of the standard form agreement entered into by its dealers and had applied for an exemption under Article 85(3). The standard form agreement contained no export prohibition and simply prohibited BMW dealers from selling new BMW vehicles to non-approved dealers.<sup>32</sup> Although finding that the action of BMW Belgium, the Dealers' Advisory Committee, and the dealers who signed the circular, violated Article 85(1), the Commission emphasized its willingness to exempt selective distribution systems in the motor industry under Article 85(3) and regarded the inherent restrictions on competition of such agreements as necessary.<sup>33</sup> However, the Commission stressed that there must not be any other restriction on the freedom of consumers to buy new cars anywhere in the Common Market or to effectuate such purchases through agents. "The export prohibition concerned . . . sought to eliminate such pressures (specifically, competitive pressures to react to differing price structures) and insulate the market operated by Belgian dealers for new BMW vehicles from the markets operated by other dealers for these vehicles in the Common Market."<sup>34</sup>

The Court of Justice rejected the appeal of BMW Belgium and the Belgian dealers.<sup>35</sup> BMW Belgium first complained that the proceedings could not be initiated on the basis of the complaints of the two German dealers. The Court disregarded this argument because the Commission was entitled to institute proceedings under its own initiative.<sup>36</sup> The Court also rejected BMW Belgium's contention that the circulars were only intended to remind the Belgian BMW dealers of the prohibition on selling to non-approved dealers. The Court concluded:

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cordingly, the fines were reduced. The dealers were fined for their negligence in signing the circulars which they should have realized went beyond the needs of a selective distribution system. Thus, BMW Belgium was fined 150,000 units of account (approximately 7,500,000 Belgian francs); the eight dealers on the Advisory Committee were fined either 2,000 or 1,500 units of account for supporting BMW Belgium's move for an export ban; the other dealers were fined a minimum of 1,000 units of account for signing the circulars.

<sup>31</sup> See notes 4-5, *supra*.

<sup>32</sup> *BMW Belgium N.V.*, *supra* note 1, at 33.

<sup>33</sup> Most of the clauses in the BMW Belgium agreement are similar to the distribution agreement of BMW Germany which was exempted by the Commission because there was no export ban. See note 23, *supra*.

<sup>34</sup> *BMW Belgium N.V.*, *supra* note 1, at 41.

<sup>35</sup> *BMW Belgium N.V.*, *supra* note 10, at 69.

<sup>36</sup> *Id.* at 58.

The circular from BMW Belgium of 29 September 1975 and the circular from the Belgian Dealers' Advisory Committee of the same date, considered according to their tenor and in relation to the legal and factual context in which they are set and in relation to the conduct of the parties, indicate an intention to put an end to all exports of new BMW vehicles from Belgium.<sup>37</sup>

Furthermore, the Court was not convinced by the applicants' position that, in spite of these circulars, Belgian dealers continued to sell new BMW vehicles abroad. The Court noted that the information supplied by BMW Belgium in regard to this argument was not persuasive, because the data supplied to the Court concerned only twenty-eight cases out of the fifty-nine cases of re-exportation of which BMW had knowledge between October 1975 and February 1976.<sup>38</sup>

The dealers' argument that they were unaware of a violation of the law or agreed to export prohibitions only under pressure was also rejected by the Court, which found that the dealers subscribed to the agreement by consenting to the circulars. The Court agreed with the Commission that the dealers were at least negligent. However, the Court concluded that the Advisory Committee and BMW Belgium knowingly violated the provisions of Article 85(1).<sup>39</sup>

The Court dismissed the application entirely and upheld the fines imposed by the Commission.<sup>40</sup> The dealers claimed their fines were unjustified because, in previous decisions in which fines were imposed for violation of Article 85(1), the Commission had never penalized dealers but only those granting the dealership. Thus, by treating the Belgian BMW dealers more severely than it had treated dealers in the past, the Commission discriminated against the Belgian dealers. The Court rejected this argument, stating that "the fact that in similar previous cases the Commission did not consider that there was reason to impose fines on resellers as well cannot deprive it of such a power expressly

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<sup>37</sup> *Id.* at 62. Although the circular begins with a reminder of the terms of the dealership agreement concerning sales to non-approved dealers, the circular does not distinguish between non-approved dealers who are not entitled to supplies from Belgian BMW dealers, and dealers who, by virtue of their status as agents, are entitled to such supplies. Moreover, BMW Munich specifically warned BMW Belgium that no action could be taken against dealers merely because they had re-exported cars. Yet, it was not until February 1976, four months after the first circular, that BMW Belgium sent a new circular to all its dealers stating that the September circular should be regarded as void.

<sup>38</sup> *Id.*

<sup>39</sup> *Id.* at 64.

<sup>40</sup> *Id.* at 69.

granted to it . . . where the conditions required for the exercise thereof are satisfied."<sup>41</sup> The applicants also were ordered to pay the costs of the Commission corresponding to the amount of the fine imposed upon it expressed as a percentage of the total fines.<sup>42</sup> The decision of the Court of Justice insures that consumers and import agents will continue to be able to obtain new automobiles outside their Member States, thereby taking advantage of substantial price differences within the Community.

The Commission has confirmed that selection of dealers by reference to their technical abilities does not come within Article 85(1) as long as the criteria are applied without discrimination, such criteria being objectively required in order to insure appropriate distribution and after sales service.<sup>43</sup> However, in regard to the partitioning of national markets by export prohibitions, the Community has sought to maintain competition between recognized resellers in different Member States with respect to products covered by selective distribution systems. The aim of the Commission is to "prevent excessive prices by insuring that demand in a Member State can be satisfied by supplies from another Member State under more favorable conditions. . . . Resellers must be free to take advantage of any price difference in a neighboring country in order to buy their products there at lower prices."<sup>44</sup> The *BMW Belgium* decision illustrates that the selective distributorship is an accepted mode of distribution in the Community if it does not hinder competition by an export prohibition. Unless the effect of restrictions is appreciable, it is unlikely that the Commission will intervene. Workable competition, although subject to some restriction, will be achieved through exemptions of selective distribution agreements under Article 85(3).

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<sup>41</sup> *Id.*

<sup>42</sup> *Id.* at 70.

<sup>43</sup> E.E.C. COMPETITION LAW 40 (B. Beckerleg ed. 1978).

<sup>44</sup> E.E.C. COMMISSION, FIRST REPORT ON COMPETITION POLICY, *supra* note 26, at 61-62.

