



adidas abandons ban on sales via online marketplaces

Sector:	Sportswear, sports shoes, sports articles, sportstyle leisure clothing
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The Bundeskartellamt has conducted administrative proceedings against adidas AG (adidas) on account of the conditions it set for the online sale of its products, especially its ban on sales via online marketplaces. The proceedings could be closed on 27 June 2014 after adidas had amended its sales conditions so that they comply with competition law.

As one of the largest manufacturers of sports articles worldwide, adidas operates a selective distribution system in which its products may only be sold to final customers through authorised retailers. In April 2012 adidas informed its retailers of its revised guidelines for online sales, so-called e-commerce conditions, which were applicable from 1 January 2013. These included among other things a ban on the sale of adidas products via so-called open marketplaces on the internet. The company named the following criteria of what constituted an open marketplace: the trade between private consumers (C2C), the trade with and sale of used and/or damaged goods and the offer of the same product by several sellers. Well-known platforms like eBay and Amazon Marketplace, but also others such as Rakuten.de, Hitmeister.de and meinPaket.de fulfilled these criteria. The company also demanded that its retailers design their websites in such a way that end consumers could not call up the site via or through a third-party platform if the logo of the third party is visible. This rule also had the effect of a ban on sales via online marketplaces. However, sales via so-called closed marketplaces such as Otto.de and Zalando.de, where individual retailers can integrate some of their products into the online shop of the platform operator, were allowed.

The Bundeskartellamt received several complaints from specialist sports retailers, which, in addition to selling goods in their own brick-and-mortar and online shops, also sell sports articles on open marketplaces. The Bundeskartellamt initiated administrative proceedings to examine whether the rules which adidas set in its conditions for sale were compatible with Art. 101 of the Treaty on the Functioning of the European Union (TFEU) and § 1 of the Act against Restraints of Competition (*Gesetzes gegen Wettbewerbsbeschränkungen (GWB)*). As part of its

investigations the authority questioned approx. 3,000 retailers and approx. 90 competitors (manufacturers of sports articles) of adidas AG as well as operators of open and closed marketplaces. The examination focused on whether the restriction of competition resulting from a per se ban on the use of online marketplaces is outweighed by sufficient efficiency gains which benefit the consumer. This necessary weighing of disadvantages and advantages under competition law reflects the economic fact that for many products selective distribution systems are effective and useful tools for increasing economic efficiency within a distribution chain because they facilitate better coordination between the companies concerned. They can also be used to solve so-called free-riding problems. These arise, for example, if some retailers choose not to invest in the quality of their sales services (e.g. advisory services, product presentation) because of individual profit considerations and attract demand away from those retailers making such investments by offering lower prices. As the investments of a retailer interested in improving its sales quality do not pay off in this case, there is less incentive for it to offer such services, although from the manufacturer's perspective and in particular also in the consumer's interest, this would be desirable. On the other hand, with the help of a selective distribution system the manufacturer can ensure that all the retailers operating within the system satisfy certain minimum quality requirements. These can include requirements on the minimum size and design of the brick-and-mortar or online shop, opening times, design and range of products, standards for the advisory staff, brand presentation and advertising measures. This ensures a uniform brand presence ("brand experience").

- **Affected markets and market shares**

Market investigations have shown that several markets are affected. These are to be differentiated between sportswear for use in sports and sporty lifestyle clothing. The investigations focussed on the sportswear market. The results of the investigations suggest that for some types of sports separate markets can be assumed for the respective sportswear. In particular, according to a preliminary estimation, football clothing and shoes constitute separate markets. In the case at hand it could be left open whether separate markets are also to be assumed in the case of clothing for other team sports, running and training/fitness.

As adidas reaches market shares of over 30 % on the markets for football clothing and shoes and on some other markets in Germany, Regulation (EU) No. 330/2010 (Vertical Block Exemption Regulation (BER))¹ is not applicable to its distribution agreements. With regard to

¹ COMMISSION REGULATION (EU) No 330/2010 of 20 April 2010 on the application of Article 101(3) of the Treaty on the Functioning of the European Union to categories of vertical agreements and concerted practices (vertical BER).

these markets it was examined whether the agreements in these markets fall under Art. 101 (1) TFEU and whether Art. 101 (3) TFEU applied.

- **Restriction of competition within the meaning of Article 101 (1) TFEU /§ 1 GWB**

The Bundeskartellamt has come to the preliminary conclusion that in the case at hand the *per se* ban on sales via online marketplaces constitutes a restriction of competition within the meaning of Article 101(1) TFEU and § 1 GWB.

Selective distribution systems generally restrict competition in the sale of the brand products of a manufacturer (intra-brand competition) because only those retailers are admitted to the distribution system which fulfil the manufacturer's selection criteria and only authorised retailers are allowed to sell the product to final customers and other authorised retailers. Under certain conditions these restrictions of intra-brand competition can also negatively affect competition between the products of competing manufacturers (inter-brand competition). On the other hand, according to ECJ case-law, selective distribution systems do not pose a restriction of competition under Article 101 (1) TFEU if the resellers are selected according to objective criteria of a qualitative nature as long as these criteria are applied in a uniform and non-discriminatory manner. In addition, the special nature of the product must necessitate such a distribution network to preserve its quality and ensure its proper use. Furthermore the criteria laid down should not go beyond what is necessary (so-called "Metro Criteria"; ECJ, ruling of 25.10.1977, case 26/76, coll. 1977, 1875, "Metro I"; recent ECJ ruling of 13.10.2011, C-439/09, "Pierre Fabre", para. 41). It should be examined whether the individual clauses of the selective distribution system, in this case the *per se* exclusion of open online marketplaces, are necessary to ensure the quality of distribution.

However, in the Bundeskartellamt's view, a ***per se* ban on sales via online marketplaces** is not a qualitative criterion which is necessary to ensure the quality of the products concerned and the quality of their distribution. Rather, specific distribution channels are excluded *per se* without any consideration of qualitative criteria, i.e. in respect of the retailer's shop on the platform or the sales environment. In the present case there were no indications that the general functionality of open marketplaces, irrespective of their specific design, would necessitate a general ban on sales in order to safeguard the quality or distribution of the sports articles concerned. In any case, there is generally the less restrictive possibility of setting specific rules on how the contract products should be sold.

The selective distribution system with its *per se* ban on (sales via) online marketplaces also significantly restricts competition by limiting the possibilities of authorised retailers to reach more

and other customers over the internet. Large and well-known retailers may depend less or not at all on their presence on online marketplaces because they already have their own well-established online shops. However, for small and medium-sized specialist retailers which are often known for their particularly high-quality distribution services, a ban on online marketplaces makes access to new customer groups difficult. For these retailers the possibility to operate their own online shop is not sufficient to market adidas products beyond the radius of their brick-and-mortar shops. Their online offers are very difficult to find if they are not allowed to use online marketplaces. Many retailers which, unlike larger players such as Zalando and Galeria Kaufhof, cannot afford expensive national advertising campaigns, depend on the customer reach of online marketplaces in order to target the relevant customers for their products. Many internet users begin their search for specific products directly on the marketplace operator's website which offers a wide variety of search functions. Apart from their presence on open marketplaces, retailers can be found by consumers in the internet mainly via listing and advertising on search engines. However, the online shops of smaller retailers have little chance of appearing under their own URL in the upper section of the results list. The prominent places are taken by adidas' own online shop and the largest retailers or closed marketplaces which, according to the results of the investigations of specialist stores, are regarded as their strongest competitors. However, the open marketplaces also normally appear here, from which the customer can easily find the offers of smaller specialist retailers. Online marketplaces are also favoured by end consumers because of their simple and safe payment methods and the department store character of the marketplaces (one-stop shopping). By repeatedly purchasing via his customer account on the online marketplace the customer has built up trust which is not directly transferable to an unfamiliar online shop of a sports specialist. This means that even if they do find the independent online shop of a retailer in the internet, customers are less prepared to buy products there because of the lack of personal experience and ratings by other users.

In the Bundeskartellamt's view the restraint of competition affects not only intra-brand competition but also competition between different sports article brands. The different sports article markets have a relatively high concentration of suppliers. Restrictions of competition in the distribution of a certain sports article brand can therefore have relative price effects which also weaken competition for other brands. In the case at hand the anticompetitive effects are further increased by the fact that other important producers of sports articles have also agreed on similar rules of sale. Due to this widespread restriction, competition between the brands is also affected.

- **No exemption under Article 101 (3) TFEU and § 2 GWB.**

An agreement which is subject to prohibition under Article 101 (1) TFEU can be exempted under Article 101 (3) TFEU if it contributes to improving the production or distribution of the goods or to promoting technical or economic progress while allowing consumers a fair share of the resulting benefit. Such agreements should also not impose restrictions on the companies concerned which are not indispensable to achieving these objectives or offer them the possibility of eliminating competition in respect of a substantial part of the products in question.

After a preliminary assessment the Bundeskartellamt concluded that adidas' per se prohibition of online marketplaces did not qualify for exemption under Article 101 (3) TFEU. Such a prohibition was not expected to produce sufficient efficiency gains and allow consumers a fair share of the resulting benefit. In addition, a per se prohibition did not fulfil the criterion of indispensability.

For many years adidas has operated a selective distribution system. This in its entirety was not the subject of examination as there was no indication of serious restrictions of competition. The question at issue was not the overall advantages of the selective distribution system but possible additional efficiency gains which could be generated by the per se ban on sales via online marketplaces. The focus of the examination was to establish whether the marketplace ban which was introduced in addition to the quality requirements for the design of an online shop could be perceived as a means to transfer the efficient quality criteria applying to brick-and-mortar sales to online sales.

In the Bundeskartellamt's view in this particular case the protection of the retailers from increased price competition which might be achieved by a marketplace ban did not improve distribution and created no efficiency gains within the meaning of Art. 101 (3) TFEU. Although reduced price competition can be advantageous from the retailers' point of view, higher prices for the sports articles concerned is not an improvement for end consumers. In this context not only adidas' general marketplace ban but also its requirement that only one retailer may offer the product on an authorised online platform were viewed with criticism. In the Bundeskartellamt's view the aim of such a rule could only be to prevent a direct comparison between the retailers' offers and hence weaken price competition.

A general ban on marketplaces is also not the appropriate way to address a potential **free-rider problem**. Firstly, free riding on the services provided by retailers offering an appropriate degree of advisory services, is not a problem which is peculiar to online marketplaces but is a general problem which applies to both sales over the internet as well as brick-and-mortar sales. The

vertical free rider problem between manufacturers selling directly online and retailers (manufacturer opportunism) is also an important aspect. The extent of the problem can vary in particular in terms of the search and time costs incurred by the end consumer. These are generally lowest on open marketplaces and highest in brick-and-mortar sales. However, consumer surveys show that free-riding occurs in both directions in online and offline sales. Irrespective of the distribution channel used, an efficient distribution system has to ensure that it provides retailers with incentives to invest in brand presentation and customer advice.

From the consumers' perspective it would seem advantageous if in their search for adidas products on online marketplaces they come across the offers of authorised retailers which meet the requirements of the brand manufacturer. Requirements set within the selective distribution system can ensure that these retailers fulfil the quality standards for the sale of adidas products on open marketplaces as well and that end customers can clearly recognise that they are authorised offers. This should also be in the interests of specialist retailers which are active in online sales. During the proceedings no protective effect could be observed from the general marketplace ban for specialist retailers operating within the selective distribution system. During the investigations numerous complaints were received from authorised specialist retailers which felt at a competitive disadvantage by the exclusive presence of non-authorised retailers on open online marketplaces as a result of the ban.

Protecting the brand image can be in the justified interest of the manufacturer and also in the interest of the final customer. In the case of the sports articles in question however, it could not be assumed that every sale via open platforms, irrespective of the type of sales environment, was likely to significantly harm adidas' brand image. Protecting its brand image cannot be used by a manufacturer as a general argument in order to justify additional restrictions to competition. The selective distribution system already imposed quality requirements to protect the brand image. Their implementation in online shops under the manufacturer's own URL and closed marketplaces shows that these also applied to online sales. Although the application of the criteria to open marketplaces required some additional adjustments, these were certainly feasible in this particular case.

In the Bundeskartellamt's view there was no indication that the per se ban created **any additional efficiency gains** beyond the implementation of the other requirements for online sale. If a completely unregulated online sale had been taken as a basis for comparison, the argument that the general ban created efficiency gains may have been justified. However, even in this case an exemption under Art. 101 (3) TFEU would not have been possible because a general ban was not indispensable for achieving these efficiency gains.

Furthermore, in the authority's view, **consumers** were unlikely to have a **fair share** of the possible efficiency gains, if any could be assumed at all. Manufacturers argue that only a marketplace ban can allow consumers a satisfying a shopping experience in keeping with the brand image and the necessary advice. However, this does not seem to correctly reflect market reality in view of the growing online trade and cross channel distribution. The willingness of a consumer to pay for the different combinations of product features, advisory services and sales environment differs from one consumer to another. Firstly, it is apparent that the demand for advisory services varies according to the individual categories of sports articles. In the retailer survey, for example, the **demand for advisory services** was clearly higher for outdoor wear than for fan wear. Secondly, the need for advisory services for one and the same product varies from one consumer to another. Some consumers appreciate the personal contact with sales staff, others prefer the ratings given by other purchasers in the internet or they already have all the purchase-relevant information. Consumers reveal their different preferences in their purchasing behaviour. The high number of online marketplace users shows that many consumers appreciate this distribution channel. The survey of retailers shows that the share of turnover achieved by retailers which in addition to their online-shops under their own URL have at least one shop on marketplaces, is higher via their marketplace shops. It seems inappropriate for adidas to refer internet-friendly consumers wishing to buy adidas products via their customer account on an online marketplace to its own online shop, closed marketplaces such as Zalando or brick-and-mortar stores with the argument that these would offer a better purchasing experience. These consumers had the possibility to buy via these channels before the open marketplaces were prohibited but decided to buy via the online marketplaces nevertheless. The group of consumers which prefer to buy from a brick-and-mortar shop or in adidas' official shop already had the possibility to do so. The purchasing possibilities for this consumer group remained unchanged after the marketplace ban.

When consumers are deprived of their preferred purchase channels, it is unlikely that they will benefit from this measure unless this is indispensable to maintain the advisory services offered by retailers within the selective distribution system. As already illustrated, a general ban on marketplaces is, however, not an appropriate way to prevent free-riding. In order to reduce coordination problems within the value chain it is necessary to create incentives within the selective distribution system which ensure that advisory services are maintained. In other words it should be ensured that authorised retailers wishing to sell their products via marketplaces also provide adequate advisory services.

The criterion that the restraints of competition have to be **indispensable** to achieve efficiency gains played a particularly significant role in the examination of the marketplace ban. Even if

one were to assume that per se bans on sales over online marketplaces could solve existing coordination problems within the value chain, which in the Bundeskartellamt's view did not apply in the case in question, these would not be indispensable in order to achieve any positive effects. In contrast to a general ban on marketplaces, quality requirements on the type and manner of marketplace distribution are a milder and less anticompetitive means to produce these effects. The most efficient way to solve any problems is to directly address them by means of quality requirements. In the course of the proceedings adidas gave an account of in its view qualitative defects in the sale of its products on various online marketplaces. Adidas has addressed these plausible areas of criticism with concrete specifications in its new guidelines on the design of shops on marketplaces and search procedures on third party platforms. The company demands that in a brand-specific search for adidas products on online marketplaces primarily adidas products should appear in the search results. This is not only in the interests of the brand owner but also of customers searching for brand products. Although the requirements are only binding on authorised adidas retailers, they are nevertheless expected to have an around positive effect on the presentation of goods on online marketplaces.

Since the restraint of competition was not indispensable it could be left open in this case whether the criterion of Article 101 (3) TFEU that competition on the affected market may not be eliminated, was satisfied. However, adidas' strong market position and the relatively high concentration on the different sports articles markets were taken into account in the competitive assessment of the case. If a company like adidas sets excessively restrictive conditions within its selective distribution system and thereby appreciably restricts intra-brand competition, this also has negative effects on inter-brand competition. Increased end customer prices for adidas products also reduce competitive pressure on other brands with the result that the price level for the sports articles concerned can generally rise. The fact that other sports articles manufacturers have introduced similar restrictions in their selective distribution systems additionally strengthens this anticompetitive effect.

- **Further points of reference**

Moreover, it would make sense to similarly assess the per se ban on sales via (open) online marketplaces in markets in which adidas does not exceed the 30% market share threshold in accordance with the vertical BER applicable to the agreement. In its preliminary assessment the Bundeskartellamt holds the view that a differentiation should be made between quality requirements which the manufacturer can set for the sale of its own products and rules which target internet distribution per se and which as serious restraints of competition do not fall under the block exemption regulation of the vertical BER from the outset. In the Bundeskartellamt's

current assessment these include requirements which significantly restrict sales by authorised retailers to final customers in a selective distribution system and which do not affect online sales or brick-and-mortar sales in the same way nor help to maintain or improve the quality of distribution. It would seem that this applies to a per se ban on sales via online marketplaces because the results of the investigations show that there are no qualitative reasons for a general ban regardless of the specific design of the marketplace, as indicated above.

In addition to the changes on platform use, adidas has modified its conditions of sale in a number of other aspects. In the Bundeskartellamt's view an important aspect is the freedom of each retailer authorised to sell adidas products to advertise the products with the help of **search engine advertising**. In its revised e-commerce conditions adidas clarified that all its authorised retailers are free to use adidas brand related terms as search words for search engine advertising such as Google AdWords. With adidas' complete elimination of its ban on third party platforms and of the requirement that only one retailer per product is authorised to sell on a platform as well as its clarification on search engine advertising, the Bundeskartellamt's competition concerns about adidas' ecommerce conditions could be dispelled.