

## The New Motor Vehicle Block Exemption A Better Hand for the Dealer?

### What is the new Block Exemption?

Motor vehicle block exemptions were first introduced in 1985 as an attempt by European legislators to restrict the amount of control that European car manufacturers could impose on their dealer networks. They have always been a balancing act between restricting the choice of the ultimate consumer and encouraging car manufacturers to invest in the industry. In the middle stand the dealers and it is they who have generally benefited least from the regulation in the new car industry. The easing of restrictions on dealers is one of the main tenets of the new Block Exemption.

It took effect from 1 October 2002. Block exemptions are immediately effective under national law, although a one-year transition period has been built in for most of this Block Exemption. There is a further transitional period ending on 30 September 2005 in relation to "location clauses" that restrict dealers from setting up in different territories.

### Why do Block Exemptions exist?

The general rule both across the States of the European Union and within each State itself is that anti-competitive practices are prohibited unless the advantages of permitting them outweigh their anti-competitive effect. Block exemptions are an attempt by the European legislators to recognise that there are certain situations in which a particular type of agreement or sector merits a special dispensation. There are currently a number in place.

Anti-competitive practices take many forms but the focus for the enforcement bodies is two-fold:

- abuses of a dominant position, where market share exceeds 40%; and
- agreements which have the object or effect of restricting trade between member states

This Information Sheet is primarily concerned with the second of these, specifically those agreements between car manufacturers and their dealer networks. Such agreements are called vertical agreements because they are agreements between parties at different levels of the chain of supply.

### Why does this industry need a specific block exemption?

Although in Europe there is a block exemption in place in relation to vertical agreements generally, the European Commission has taken the view that the motor vehicle industry warrants sector-specific

regulation because the distribution of new cars poses particular problems.

Manufacturers have sought to protect their market share and investment by controlling the activities of dealers. The traditional defence of manufacturers is that this means a better standard of quality and safety for the customer and the comfort of knowing that after-sales servicing is carried out by personnel trained by the manufacturer.

### What changes does the New Block Exemption bring into effect?

The new Block Exemption is detailed, though less so than the explanatory note that comes with it. It makes extensive changes (and some would say, unnecessarily extensive changes) that are intended to open up competition in the new car sector by giving dealers more freedom and the customer greater choice.

The Schedule attached provides a basic comparison between the old and the new position.

### Competition Law

To have the benefit of the block exemption (that is, to ensure that an agreement containing certain restrictions is enforceable) the dealer agreements must meet certain familiar competition rules:

- (a) the agreement as a whole must be drafted to fit within the block exemption. Any restrictions that are not dealt with by the block exemption would fall to be analysed under the general competition regime relating to vertical agreements;
- (b) new market share thresholds (see Schedule);
- (c) the benefit of the block exemption is lost in relation to the entire agreement if there are any hard core anti-competitive provisions, such as price fixing;
- (d) the benefit of the block exemption will also be lost in relation to any non-permitted obligations such as restrictions on dealers from selling cars or spare parts of competing manufacturers.

### How does the industry view the changes?

There is no doubt that views on the new block exemption will differ between manufacturers, dealers, authorised repairers and customers. The early view is that the block exemption is unnecessarily complex. This is because one of the driving forces behind the changes has been the growth of internet sales, broker arranged sales and car supermarkets. It was proving hard for

customers to buy cars through these, often cheaper, routes because manufacturers could control to whom dealers sold vehicles, thereby artificially keeping the prices up. By this analysis, the block exemption needed only to remove this restriction but as the Schedule shows, there are many more fundamental changes.

### **How will the block exemption affect the manufacturers?**

The cynical view is that in the medium to long term, manufacturers will retain the same level of control by finding new ways to exert pressure on dealers and to control prices.

Some manufacturers have already terminated their dealer agreements and are looking to agree new terms that are likely to include far more onerous criteria to be met. Others are buying out their dealer networks in order to retain control over sales.

Generally, as dealers will have the right to set up additional outlets anywhere within the EU, price fixing should be reduced as dealers will be able to source stock from lower cost EU states. This option though may over time become extinguished as the tax regimes of all EU states become harmonised.

In addition, manufacturers will lose their monopoly and profits from the sale of parts.

In defence of the manufacturers, establishing dealer networks involves a high level of financial investment and reducing their control over the distribution of cars throughout the EU is unlikely to reduce prices in the long term.

It is more likely that as a result of the new Block Exemption manufacturers will opt mostly for a selective distribution system as the restrictive benefits of allocating an exclusive territory have been eliminated.

### **What about the dealers?**

Dealers, other than exclusive dealers, have been given freedom to operate where they wish and some dealers will inevitably benefit from this. Dealers, too, though need a high degree of financial support to set up a single dealership, let alone a network across the EU states.

Those that manage this will increase sales and buying power. One view is that this means the arrival of a new breed of super-dealer, with the market being dominated by only large outlets, offering many different brands of cars. Ironically,

this ultimately could restrict the choice of the customer.

### **Are there likely to be any benefits for the customer?**

Customers will always need to buy cars and there are undoubted benefits to them of opening up the entire EU to greater choice and competition.

As things currently stand, although value and choice are essential (and there is no doubt that these things are currently lacking in the European Market) for what is a significant financial outlay, the customer will want the security of a recognised brand and the standards that the brand represents.

This may mean that there will be different markets for different types of vehicle. The luxury brands may continue to be sold in the same way as now, so that the customer will have that security that goes with a luxury brand. At the cheaper end of the range, it is likely that car supermarkets will flourish from the greater availability of vehicles.

### **Summary**

The EC has shown that it is not afraid to take action against manufacturers engaged in anti-competitive practices. This is currently a hot topic in Europe and manufacturers will certainly need to ensure compliance with the new regime if they are to avoid the fines that can be imposed of up to 10% of world-wide turnover.

This information sheet has been prepared by the Commercial Group at Thomson Snell & Passmore to highlight some key issues relating to the new motor vehicle block exemption. It is intended to be for general guidance only and is not a substitute for specific advice. It is based upon our understanding of the position as at June 2003 and may be affected by subsequent changes in the law.

Should you require any specific legal advice on the issues covered, please e-mail James Partridge at [james.partridge@ts-p.co.uk](mailto:james.partridge@ts-p.co.uk) or call on 01892 510000.

The Commercial Group at Thomson Snell & Passmore provides a full range of services in relation to competition law, commercial contracts, corporate transactions, e-commerce, and intellectual property issues.

# Schedule

PREVIOUS SYSTEM	NEW SYSTEM
<b>Distribution Systems</b>	
Manufacturers were free to combine exclusive and selective distribution systems giving dealers a local monopoly if they met criteria set by the manufacturer. As a result the manufacturer had a large degree of control over the business of the dealer	Manufacturers must now choose in each EU state between an <b>exclusive distribution</b> system (where the dealer would get a designated territory in which to focus its attention but does not need to meet the manufacturer's selection criteria) or a <b>selective distribution</b> system (where the manufacturer can choose between a <i>qualitative system</i> and a <i>quantitative system</i> )  <ul style="list-style-type: none"> <li>• <b>Qualitative system</b> means that the manufacturer can impose criteria to be met by the dealer, such as training requirements for sales personnel and requirements relating to products on display</li> <li>• <b>Quantitative system</b> means that the manufacturer can impose criteria that directly limit the number of dealers in a given area</li> </ul>
A dealer's share of sales in a given market could be limited by the manufacturer refusing to grant additional contracts to the same dealer	This is no longer permitted for contracts based on selective criteria as the selective system dealers cannot be limited by territory
	Selective system dealers are able to sell their dealership on to a third party of their choice within the same distribution system
<b>Market Share Test</b>	
No market share threshold was specified for the benefit of the old block exemption to apply	For the benefit of the new block exemption to apply the manufacturer's market share must not exceed: <ul style="list-style-type: none"> <li>• 30% for exclusive distribution systems</li> <li>• 40% for quantitative selective distribution systems</li> <li>• None for qualitative selective distribution systems because they are not seen as having an anti-competitive effect</li> <li>• Where market share exceeds these thresholds general principles of competition law will apply to the dealer contracts</li> </ul>
<b>Cross Border Sales</b>	
Exclusive distributors were restricted from actively selling outside their territory	Manufacturers cannot restrict onward sales (for example, to consumers in another member state) although exclusive dealers will still not be permitted to open dealerships or to appoint sub-dealers or agents outside their territory
	Dealers in selective systems will be able to set up secondary outlets anywhere in the EU from 2005 as long as those outlets meet the same selective criteria
<b>Multi-branding</b>	
Dealers were generally not permitted to sell more than one brand of car from the same showroom	Dealers may sell other brands from the same showroom as long as each brand has its own segregated space
Manufacturers could insist on brand specific personnel	Brand specific personnel are not permitted

<b>Pricing</b>	
Manufacturers could indirectly control dealers' selling prices and gross margins	It is no longer permitted for manufacturers to control selling prices or to limit sales
<b>Servicing &amp; After Sales</b>	
Dealers were required to provide both a sales and after-sales service	After-sales services can be subcontracted by dealers to authorised repairers who meet appropriate standards
Manufacturers could insist that dealers conform to standards such as requiring that the repair facilities must be on the same premises as the sales facilities	Dealers can now simply notify customers of the location of after-sales service suppliers although they will be responsible for the satisfactory performance of sub-contracted service/repair suppliers
Manufacturers could limit the number of authorised repairers and decide on their location	Manufacturers cannot limit the number of authorised repairers who fulfil the qualitative criteria set by them
Manufacturers could dictate charge out rates	As repairers can now be independent this will not be possible
Spare parts were only available through the manufacturers, keeping prices up	Dealers and authorised repairers can source parts from anywhere except in relation to warranty parts
Little choice for the consumer of different spare parts within the repair shop of an authorised repairer.	Consumers will now be able to choose between the spare parts supplied by the vehicle manufacturer, the spare part manufacturer or matching quality spare parts supplied by another spare part producer
<b>Information</b>	
Access to technical information was not easily accessible and not adapted to the needs of independent repairers	Access to technical information has improved for all operators involved in repair training and technical assistance.
<b>Termination</b>	
Termination of a dealership could be given without providing reasons and subject to a 2 year notice period.	For contracts of indefinite duration, 2 years' notice is still required but the manufacturer must give clear reasons for termination in writing as to allow for the matter to be referred to an independent adjudicator, if necessary
	Fixed term agreements must be for a minimum of 5 years at least and must provide a minimum notice period of 6 months