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Electronic Commerce, Social Media and Franchising

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Introduction: the increasing importance of electronic commerce

Some general trends and figures – pre-covid-19

The European Union is one of the largest electronic commerce (e-commerce) markets in the world today. We are truly a digital society, all the more so since the covid-19 pandemic, and businesses increasingly interact online with customers and business partners. Browsing, chatting and online shopping are everyday activities that use information and communication technologies.[2] The internet is the cornerstone for e-commerce web sales (via a website or app).[3]

Looking back to 2017, 16 per cent of EU businesses reported generating web sales online (via a website or app). Ireland reported the highest number of businesses with web sales (25 per cent), followed by Denmark and Germany (both 23 per cent), and Sweden (22 per cent).[4] The share of total EU turnover generated from such web sales amounted to 5 per cent. Ireland also had the highest share of total turnover generated from web sales (15 per cent) followed by Belgium (11 per cent), and Sweden and the United Kingdom (both 8 per cent).

Belgium registered the highest share of business-to-business (B2B) web sales (7 per cent), followed by the Czech Republic and Denmark (both 5 per cent).[5] The share of turnover generated

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2 'Digital economy and society in the EU, A browse through our online world in figures', Eurostat 2018 edition, available at: https://ec.europa.eu/eurostat/cache/infographs/ict/2018/index.html, visited 29 January 2021.

3 Apps are typically available on mobile phones or equivalent devices and, therefore, a separate 'mCommerce' channel is sometimes distinguished. For the purposes of this chapter such mCommerce is considered to fall within e-commerce.

4 Businesses with web sales (as percentage of EU businesses), 2017.

5 Turnover from web sales: B2B (as percentage of total turnover), 2017.

from business-to-consumer (B2C) sales was highest in Ireland (12 per cent), followed by the United Kingdom (4 per cent), and Belgium, Spain, the Netherlands and Sweden (all 3 per cent).[6]

More recent trends and figures

Of course, these statistics were generated before the global covid-19 pandemic and the ensuing lockdowns.[7] Without examining detailed statistics we are all now acutely aware of the effect that the pandemic has had on bricks-and-mortar retail. The pandemic has accelerated technology adoption in many sectors and increased online shopping. One of the clearest illustrations is in the United Kingdom where Fashion retailer Boohoo is buying the Debenhams brand and website for £55m. Boohoo was not, however, interested in purchasing any of the 242-year-old retailer's remaining chain of 118 bricks-and-mortar stores.[8]

In 2019, more than three-quarters (77 per cent) of enterprises in the EU 27 had a website, with a much higher share for large enterprises (94 per cent) compared with small enterprises (74 per cent). This share was 8 percentage points higher than it had been in 2011. The highest share of enterprises using customer relationship management (CRM) applications was recorded in the Netherlands (56 per cent), Belgium (46 per cent) and Germany (44 per cent). The adoption of CRM was at a lower level in Croatia (19 per cent), Bulgaria (17 per cent), Latvia (16 per cent) and Hungary (12 per cent).[9]

The e-commerce sector inquiry

The EU Commission's 2017 e-commerce sector inquiry found that, while price is a key parameter of competition between retailers, quality, brand image and innovation are important in the competition between brands:

> *Incentivising innovation and quality and keeping control over the image and positioning of their brand are of major importance for most manufacturers to help them ensure the viability of their business in the mid to long-term.*[10]

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6 Turnover from web sales: B2C (as percentage of total turnover), 2017. All charts referred to are available at: https://ec.europa.eu/eurostat/cache/infographs/ict/2017/bloc-2b.html, visited 16 January 2020.

7 See Digital economy and society statistics – enterprises, available at: https://ec.europa.eu/eurostat/statistics-explained/index.php?title=Digital_economy_and_society_statistics_-_enterprises, visited 29 January 2021.

8 'Boohoo snaps up Debenhams brand for £55m as Asos targets Topshop', www.ft.com/content/c81e7266-984f-4c38-8543-83e6449eb79a, visited 31 January 2021.

9 Digital economy and society statistics, op cit. The data were extracted in September 2020 and the EU is planning to issue a revised report in September 2021.

10 EU Commission, Final report on the e-commerce sector inquiry, 10 May 2017, COM (2017) 229 final, paragraph 12, page 5. The final report is divided into two separate sections: the first section covers e-commerce of consumer goods, while the second focuses on e-commerce of digital content.

The sector inquiry noted both the ability of retailers to leverage online distribution models to access customers, thereby increasing the size of their potential customer base, and the potential for such initiatives to clash with the distribution and brand strategies of manufacturers.[11]

Even if certain characteristics of the franchise relationship – and notably the know-how that is transferred from franchisor to franchisee – distinguish it from reselling or distribution, replacing the word 'manufacturers' with 'franchisors' in the previous two paragraphs makes clear the challenges that franchisors, franchisees and franchise networks must meet to prosper in the new e-commerce environment. Those challenges are discussed below.

The changing online legislative context for electronic commerce

A Europe fit for the Digital Age

Within the limits set by article 5 of the Treaty on European Union (TEU)[12] the European Commission has the responsibility for adopting proposals to initiate Union legislation.[13] The President of the current European Commission (2019–2024), Ursula von der Leyen, has made the creation of a 'Europe fit for the Digital Age' one of the keystones of her Commission's policy agenda.

This led to the adoption of a package of policy reflections from the Commission in February 2020, in particular a Communication on shaping Europe's digital future in which the Commission committed to updating the horizontal rules defining the responsibilities and obligations of digital service providers and online platforms.[14] This Communication was accompanied by a Communication on a European strategy for data[15] and a White Paper on a European approach to excellence and trust in artificial intelligence.[16]

Legislative initiatives have followed, notably, the proposed European Data Governance Act (DGA),[17] Digital Markets Act (DMA),[18] and the Digital Services Act (DSA).[19] The DGA aims to facilitate data-sharing, including sharing of data among businesses and allowing personal data to be used with the help of a personal data-sharing intermediary. (The interplay with the GDPR and the (current) ePrivacy Directive is particularly important.) The DMA proposal would essentially affect the companies sometimes referred to as the FAANG[20] and Microsoft. Such companies are designated as providers of core platform services (referred to as gatekeepers) that have:

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11 EU Commission, Final report on the e-commerce sector inquiry, op cit, paragraph 14, page 5.

12 Article 5 sets out key principals of competence, conferral, subsidiarity and proportionality that limit EU legislative action. The limits of EU competences are governed by the principle of conferral. The use of union competences is governed by the principles of subsidiarity and proportionality.

13 Article 17 TEU.

14 Communication from the Commission, 19 February 2020, COM (2020) 67 final.

15 Communication from the Commission, 19 February 2020, COM (2020) 66 final.

16 White Paper from the Commission, 19 February 2020, COM (2020) 65 final.

17 Proposal for a Regulation on European Data Governance, 25 November 20 20, COM (2020) 767 final.

18 Proposal for a Regulation on Contestable and Fair Markets in the Digital Sector, 15 December 2020, COM (2020) 842 final.

19 Proposal for a Regulation on a Single Market for Digital Services, 15 December 2020, COM (2020) 825 final.

20 FAANG is an acronym that refers to five prominent US technology companies: Facebook, Amazon, Apple, Netflix and Alphabet (formerly known as Google). Arguably Microsoft, should also be mentioned – but its name does not easily fit within the acronym.

- a significant impact on the internal market;
- operate a core platform service that serves as an important gateway for business users to reach end users; and
- enjoy a durable market position (or will foreseeably enjoy such a position in the near future).[21]

The companies subject to the DMA are therefore essentially beyond the scope of this chapter – although many franchisors and franchisees as well as their customers will use the gatekeeper's services.

The DSA proposal builds on the existing e-Commerce Directive.[22] the specific objectives of which include ensuring a well-functioning internal market for digital services. Building on that framework the DSA proposal seeks to ensure optimum conditions for the provision of innovative digital services in the internal market. It defines clear responsibilities and accountability for providers of intermediary services, and in particular online platforms, (including social media and marketplaces). It also seeks to improve users' safety online. Platforms would be required to obtain, store, verify (in part) and publish information on traders using their services, thereby making the online environments for consumers more transparent.

The Geo-blocking Regulation

On 3 December 2018, new rules on geo-blocking entered into force in the EU (the Geo-blocking Regulation).[23] The rules are part of a wider package of measures under the EU's Digital Single Market Strategy,[24] aimed at boosting cross-border e-commerce in the EU.

Geo-blocking refers to online sellers' practices that restrict online cross-border sales based on nationality, residence or place of establishment. These geo-blocking practices include denying access to websites from other member states, or situations where access to a website is granted,

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21 Draft proposal for the DMA, op cit, article 3, Designation of Gatekeepers.

22 Directive No. 2000/31/EC of 8 June 2000 on legal aspects of information society services, in particular electronic commerce, in the internal market, (17 July 2000 OJ L178, page 1).

23 Regulation (EU) 2018/302 of 28 February 2018 addressing unjustified geo-blocking and other forms of discrimination based on customers' nationality, place of residence or place of establishment within the internal market, OJ L 60I, of 2 March 2018, pages 1–15.

24 On 25 May 2016, the Commission presented a package of measures designed to boost the potential for cross-border e-commerce in Europe. The main aim of the package was to break down barriers to cross-border online activity and to define a comprehensive e-commerce framework. See Commission Press Release: 'Commission proposes new e-commerce rules to help consumers and companies [gain] full benefit [from the] Single Market' of 25 May 2016, available at: http://europa.eu/rapid/press-release_IP-16-1887_en.htm, visited 16 January 2020. See also: EU Commission Communication 'A comprehensive approach to stimulating cross-border e-Commerce for Europe's citizens and businesses' COM (2016) 320 final of 25 May 2016 available from: http://ec.europa.eu/DocsRoom/documents/16804.
On 27 June 2019, the Commission issued a press release showing that 'Europeans are well aware of rules against unjustified geo-blocking', available at: https://ec.europa.eu/commission/presscorner/detail/en/IP_19_2528, visited 16 January 2020.

but the customer from abroad is prevented from finalising the purchase or is asked to pay with a debit or credit card from a certain country.[25]

Access to websites

Article 3 of the Geo-blocking Regulation bans the blocking of access to websites and rerouting without the customer's prior consent. This increases price transparency by allowing customers to access different national websites. This provision also applies to non-audiovisual services supplied electronically, such as e-books, music, games and software.

Supposing an Irish customer wants to access the Italian version of an online clothing store's website. Even though he or she types in the URL of the Italian site, he or she still gets redirected to the Irish site. Since 3 December 2018, being redirected requires the customer's explicit consent. Moreover, even if the customer gives consent to the redirection, the original version he or she sought to visit should remain accessible.[26]

Cross-border parcel deliveries

A 2018 Regulation made prices for cross-border parcel delivery services more transparent. It was also intended to make these services more affordable and to increase regulatory oversight of the EU parcel market.[27] It became applicable as of 22 May 2018.[28] By making it easier for consumers and smaller companies to buy and sell products and services online with confidence across the EU, it is expected to boost e-commerce within the EU.

Simplification of VAT rules for cross-border sales

The value added tax (VAT) e-commerce package adopted by the European Council on 5 December 2017 included several changes to the place of supply rules.[29] The purpose of these changes is to reduce the burden for small and medium-sized enterprises (SMEs) established in a member state supplying goods and services to customers in other member states. From

25 The Regulation does not apply to situations that are purely internal in a member state, where all the relevant elements of the transaction are confined to a single member state, in particular the nationality, the place of residence or the place of establishment of the customer or of the trader, the place of execution, the means of payment used in the transaction or the offer, as well as the use of an online interface.

26 See further: 'Questions & Answers on the Geo-blocking Regulation in the context of e-commerce' available from https://ec.europa.eu/digital-single-market/en/news/geo-blocking-regulation-questions-and-answers.

27 Regulation (EU) 2018/644 of 18 April 2018 on cross-border parcel delivery services, OJ L 112, 2 May 2018, pages 19–28.

28 With the exception of article 8 (penalties for infringements), which applied from 23 November 2019.

29 On 5 December 2017, the European Council adopted the VAT e-commerce package consisting of: Council Directive (EU) 2017/2455 modifying Directive 2006/112/EC (the VAT Directive); Council Regulation (EU) No. 2017/2454; and Council Implementing Regulation (EU) No. 2459/2017 modifying Regulation (EU) No. 282/2011 (the VAT Implementing Regulation).

1 July 2021, the original simplification rules[30] will be extended and will simplify VAT collection when consumers buy goods and services online from another member state or a non-EU country by introducing the possibility for the suppliers to use a VAT One Stop Shop (OSS):[31]

- the EU scheme for intra-EU supplies of telecommunications, broadcasting and electronic (TBE) services will be extended to all types of B2C services as well as to intra-EU distance sales of goods and certain domestic supplies facilitated by electronic interfaces. The extension to intra-EU distance sales of goods goes hand in hand with the abolition of the current distance sales threshold, in line with the commitment to apply the destination principle for VAT; and
- an import scheme will be created covering distance sales of goods imported from third countries or territories to customers in the EU up to a value of €150.

On 30 September 2020, the Commission published explanatory notes on the new VAT e-commerce rules. They contain extensive explanations and clarifications of the new rules including practical examples on how to apply the rules if you are a supplier or provide an electronic interface (eg, marketplace or platform) for e-commerce transactions. The explanatory notes are intended to help online businesses and in particular SMEs to understand their VAT obligations arising from cross-border supplies to consumers in the EU.[32] Guidance for traders and the member states concerning the import and export of low value consignments has also been published.[33]

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30 The original rules simplified VAT obligations for SMEs supplying TBE goods and services B2C across borders. An annual €10,000 turnover threshold was introduced on 1 January 2019, up to which the place of supply of relevant supplies of cross-border TBE services remains in the member state where the supplier is established, has his or her permanent address or usually resides. (The application of this threshold was subject to conditions.)
For supplies above €10,000, a further threshold of €100,000 was introduced in Germany, Luxembourg and the Netherlands, up to which a single piece of evidence was sufficient to determine the place of supply of TBE services (as opposed to the two required previously). In the other EU member states the threshold is €35,000. (The application of this threshold was also subject to conditions.)

31 Because of the practical difficulties created by the measures taken to contain the coronavirus pandemic, the application of the new VAT e-commerce rules has been postponed for six months. The rules will apply as of 1 July 2021 instead of 1 January 2021, giving member states and businesses additional time to prepare.

32 See generally https://ec.europa.eu/taxation_customs/business/vat/modernising-vat-cross-border-ecommerce_en. The Commission adopted the Implementing Regulation (EU) No. 2020/194 laying down details on the working of the VAT One Stop Shop on 12 February 2020. The Explanatory Notes are available at: https://ec.europa.eu/taxation_customs/sites/taxation/files/vatecommerceexplanatory_28102020_en.pdf, both documents visited on 31 January 2021.

33 https://ec.europa.eu/taxation_customs/sites/taxation/files/guidance_on_import_and_export_of_low_value_consignments_final.pdf.

Digital contract rules

The digital contract rules include two Directives:

- a directive on contracts for supply of digital content;[34] and
- a directive containing contractual rules for online sale of tangible goods.[35]

The two Directives apply from the beginning of 2022. They have the common object of removing obstacles to cross-border e-commerce in the EU (and notably legal fragmentation) in the areas of consumer contract law that cause high costs for business and low consumer trust when buying online in another country.

With the new digital content rules, consumers will be protected when digital content and digital services are faulty, and will have the right to seek remedies:

- asking the trader to fix the problem; and
- if the problem persists, obtain a price reduction or terminate the contract and get a refund.

Many of consumers' top concerns about buying goods from abroad are about contract rights. For example, what happens if:

- you don't receive the order as promised;
- you get a wrong or damaged product; or
- the product turns out to be faulty after a while, and you want it repaired or replaced.

Under the Directive for online sales of tangible goods, which sales channel the shopper uses will not be so important any more. Whether a consumer buys a new camera online or in a bricks-and-mortar shop, the consumer's rights and trader's obligations will be the same if the product proves faulty. The goods must be in conformity both with what is agreed and with what the consumer could reasonably expect. In the event of a lack of conformity, the same remedies will apply throughout the EU.

Using the e-commerce channel: how and when challenges may arise

Challenges for franchisors and franchisees

Where issues around e-commerce have not been adequately dealt with previously, they will tend to arise either on a franchise renewal or when the franchisor tries to introduce new standard terms.

Dymocks Holdings

The point is helpfully illustrated by a franchise dispute that occurred in New South Wales, Australia in 2000. Dymocks, the largest bookseller in Australia, established its franchise system in 1986. The franchise agreements at issue in *Dymocks Holdings v Top Ryde Booksellers*[36] provided an option for renewal on the terms of the Dymocks' standard form of agreement. However, when

34 Directive (EU) 2019/790 of 20 May 2019, applicable from 1 January 2022.

35 Directive (EU) 2019/771 of 20 May 2019, applicable from 1 January 2022.

36 *Dymocks Holdings Pty Ltd & Ors v Top Ryde Booksellers Pty Ltd & Ors* [2000] NSWSC 795, judgment of 11 August 2000.

the franchisor subsequently introduced a new form of agreement it precluded any claim by the franchisees to commercial participation in the franchisor's website.

The new standard form agreement that was introduced contained a definition of Dymocks' website and various acknowledgments and restrictions on the franchisee, including that:

- the franchisee must have no legal or equitable interest of any nature or description whatever in any Dymocks website or any business conducted through or any revenue derived from the operation of such website;
- the existence and operation of such website for home shopping must provide a benefit to the franchisees because it increases brand awareness by members of the public of the Dymocks name and brand; and
- the franchisee must not hold a direct or indirect interest in a website incorporating or including the word Dymocks without prior written consent from a member of the Dymocks Group.

After a challenge by the franchisee, the courts in New South Wales held that Dymocks was not entitled to defeat its original unqualified promise that its website would be the property of the advertising fund (and therefore an asset shared with the franchisees) through its new standard form agreement. The franchisees were therefore entitled to compensation on the basis that the website remained an asset of the advertising fund. Expensively, the case made its way to the Privy Council, in London, where the decisions of the trial judge and the NSW Court of Appeal were both reversed on the unusual basis that they had both 'left out of account factual matters of great importance' relevant to the issue of repudiation of the contract. The Privy Council found that Dymocks was therefore entitled to terminate the agreements.[37]

Tyre 20 v Fleet Mobile Tyres

A similar dispute arose in the *Tyre 20 v Fleet Mobile Tyres* case heard by the Court of Appeal in England in August 2006.[38] The case concerned a mobile tyre-fitting service in which the mobile fitter would travel to the vehicle in question and fit a new tyre by the roadside, in the driveway, or wherever was convenient for the customer, instead of taking the vehicle to a garage. Much of the new business was achieved by local efforts of the franchisee in its particular territory, but some came from National Account Customers managed by the franchisor. From about 1997 the defendant franchisor developed an eTyres website managed by head office staff.

The dispute that arose between the parties concerned the eTyres work, which was originally a minority element of the total balance of work. Although the eTyres work was part of the business franchised to the appellant under the franchise agreement, the defendant franchisor only

37 *Dymocks Franchise Systems (NSW) Pty Ltd v Todd (New Zealand),* [2002] UKPC 50 (7 October 2002) [2002] 2 All ER (Comm) 849, [2002] UKPC 50; from The Judicial Committee of the Privy Council Decisions.

38 *Jeffrey Stone and Lynn Ashwell (trading as 'Tyre 20') v Fleet Mobile Tyres Limited*, [2006] EWCA Civ 1209, judgment of 31 August 2006.

passed on the eTyres work after making deductions so that the work was less profitable for the appellant franchisees.[39]

In October 2004, all franchisees, including the appellants, were told that the franchisor was going to take initiatives to promote its eTyres brand. The initiatives included changing signage on the vans to identify eTyres as the principal brand with similar changes to business cards, stationery and promotions on which eTyres was to be the only branding. The appellants claimed that in result they were entitled to treat the franchise agreement as having been wrongfully terminated by the franchisor.

The Court held that it was clear that the franchisor's instructions would have prevented the appellants from effectively promoting the 'Fleet Mobile Tyres' aspect of the franchise. The eTyres part of the business would have predominated but that was a part of the business where the prices to the customer were assessed by the franchisor not by the franchisee. Whereas the franchise agreement clearly contemplated that the Fleet Mobile Tyres work was to be a significant part of the franchise business, the franchisor was effectively imposing far-reaching restrictions on the franchisee's ability to promote the part of the business where it set the sale price directly with the customer. Accordingly, the appellants were entitled to treat the franchise agreement as having been terminated by the franchisor.

Scope for improving the performance of franchising in Europe

A September 2016 paper considered how the regulatory environment of the EU impacts on franchising.[40] The core thesis of the paper was that franchising is substantially underperforming in the EU. The evidence cited for that proposition was that 83.5 per cent of franchising turnover in the EU was concentrated in only 25 per cent of the member states and constituted only 1.86 per cent of the EU's GDP.[41] (This compared unfavourably with 5.95 per cent of GDP in the US and 10.83 per cent of GDP in Australia.)

Among the criticisms levied at the position of franchising within the EU was a lack of recognition and support for multichannel sales, online sales and other commercial use of the internet.[42] In particular, the EU Commission was criticised in the paper for failing to understand the dynamic and interactive nature of the worldwide web, thus using an outmoded approach to the latest developments in electronic commerce: '[b]y seeing the Internet as a passive medium

39 The dispute about eTyres in *Tyre 20 v Fleet Mobile Tyres* illustrates the importance of potential competition between a franchisor and its franchisees for the incremental business opportunities derived from an e-commerce channel. A further practical example would be if a master food franchisor decided to offer delivery services on-line, whereas its franchisees remained limited to face-to-face contacts through their bricks-and-mortar outlets. The question of whether and to what extent to franchisors in the EU may exercise control over internet use by franchisees, as opposed to what access franchisees should be granted to online sales channels, is discussed in the next section.

40 Legal perspective of the regulatory framework and challenges for franchising in the EU, Abel M September 2016, PE 587.317. The document was prepared at the request of the Committee on Internal Market and Consumer Protection (IMCO) of the European Parliament. An earlier, more extensive, study entitled 'Franchising' was also prepared for IMCO, author, Dr Aneta Wiewiórowska-Domagalska April 2016, PE 578.978.

41 PE 587.317 op cit, Executive Summary, page 6.

42 PE 587.317 op cit, Multi-Channel Strategies, pages 19–20.

comparable to a journal or newspaper the importance of multi-channel sales strategies is totally missed'.[43]

EU franchisors: controls over internet use

The EU Vertical Agreements Block Exemption Regulation

The EU's general competition rules, set out in article 101(1) of the Treaty on the Functioning of the European Union (TFEU), prohibit restrictive agreements made between undertakings that may affect trade between member states and whose object or effect is the prevention, restriction or distortion of competition within the EU internal market. Based on previous experience, the EU Vertical Agreements Block Exemption Regulation (VBER) exempts certain contractual arrangements found in business agreements and practices from the prohibition set out in article 101(1) TFEU. It also clarifies that certain other (hardcore) clauses restricting competition do not benefit from that exemption.[44]

The Commission Guidelines on Vertical Restraints

The distinction that EU competition law makes between active and passive selling outside an allocated contract territory is well known. The Commission's Guidelines on Vertical Restraints (CGVR), which support the VBER, define passive sales in paragraph 51 as:

> *responding to unsolicited requests from individual customers including delivery of goods or services to such customers. General advertising or promotion that reaches customers in other distributors' (exclusive) territories or customer groups but which is a reasonable way to reach customers outside those territories or customer groups, for instance to reach customers in one's own territory, are considered passive selling. General advertising or promotion is considered a reasonable way to reach such customers if it would be attractive for the buyer to undertake these investments also if they would not reach customers in other distributors' (exclusive) territories or customer groups.*

The CGVR set out a number of ways in which restrictions on internet sales may restrict competition, and paragraph 52 states:

> *The internet is a powerful tool to reach a greater number and variety of customers than by more traditional sales methods, which explains why certain restrictions on the use of the internet are dealt with as (re)sales restrictions. In principle, every distributor must be allowed to use the internet to sell products. . . . The Commission thus regards the following as examples of hardcore restrictions of passive selling given the capability of these restrictions to limit the distributor's access to a greater number and variety of customers: . . . (c) an agreement that the distributor shall limit its proportion of overall sales made over the internet.*[45]

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43 Abel M, PE 587.317 loc cit. Emphasis added.

44 Commission Regulation (EU) No. 330/2010 of 20 April 2010 on the application of article 101(3) of the TFEU to categories of vertical agreements and concerted practices, OJ L 102, 23.4.2010, pages 1–7.

45 Emphasis added.

However, paragraph 54 of the CGVR qualifies the general position stated above to the extent that it recognises that quality standards may also be relevant to sales over the internet, in particular in the context of selective distribution agreements:

> [under the VBER] *the supplier may require quality standards for the use of the internet site to resell its goods, just as the supplier may require quality standards for a shop or for selling by catalogue or for advertising and promotion in general. This may be relevant in particular for selective distribution. Under the* [VBER], *the supplier may, for example, require that its distributors have one or more brick and mortar shops or showrooms as a condition for becoming a member of its distribution system . . . Similarly, a supplier may require that its distributors use third-party platforms to distribute the contract products only in accordance with the standards and conditions agreed between the supplier and its distributors for the distributors' use of the internet. For instance, where the distributor's website is hosted by a third-party platform, the supplier may require that customers do not visit the distributor's website through a site carrying the name or logo of the third-party platform.*

The CJEU's jurisprudence

Although the Commission's guidance in the CGVR is persuasive,[46] it is soft law and must be read subject to judicial interpretation of the relevant law by the Court of Justice of the European Union (CJEU) and the General Court.[47] Two significant judgments, *Pierre Fabre*[48] and *Coty*,[49] have helped throw some light on what contract terms a franchisor may (and may not) adopt to regulate its franchisees' use of internet marketing. Both cases concerned selective distribution systems.[50]

Pierre Fabre

Pierre Fabre Dermo-Cosmétique (PFDC) established a selective distribution system for certain cosmetic and personal care products under specified brands. The distribution contracts for those products stipulated that sales must be made exclusively in a physical space, in which a qualified pharmacist must be present to give advice to the customer on the product best suited to specific health or care matters.

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46 CGVR, op cit, recital (3): 'By issuing these Guidelines, the Commission aims to help companies conduct their own assessment of vertical agreements under EU competition rules. The standards set forth in these Guidelines cannot be applied mechanically, but must be applied with due consideration for the specific circumstances of each case. Each case must be evaluated in the light of its own facts.'

47 CGVR, op cit, recital (4): 'These Guidelines are without prejudice to the case-law of the General Court and the Court of Justice of the European Union concerning the application of Article 101 to vertical agreements.'

48 *Pierre Fabre Dermo-Cosmétique SAS v Président de l'Autorité de la concurrence and Ministre de l'Économie, de l'Industrie et de l'Emploi*, judgment of 13 October 2011, Case C-439/09 [2011] I-9419.

49 *Coty Germany GmbH v Parfümerie Akzente GmbH*, judgment of 6 December 2017, Case C-230/16, published in the electronic Reports of Cases (Court Reports – general).

50 For a commentary see: Botteman, Yves; Barrio, Daniel: 'From Pierre Fabre to Coty and Beyond: How Far Can Suppliers Ban Online Sales?', *Journal of European Competition Law & Practice* 2019 Vol.10 No. 9 pages 519–531.

Article 1.1 of the general conditions of those contracts required each distributor:

> *to supply evidence that there will be physically present at its outlet at all times during the hours it is open at least one person specially trained . . . to give on-the-spot advice concerning sale of the [PFDC] product that is best suited to the specific health or care matters raised with him or her, in particular those concerning the skin, hair and nails. In order to do this the person in question must have a degree in pharmacy awarded or recognised in France.*

Article 1.2 stated that the products concerned might only be sold 'at a marked, specially allocated outlet'. It was accepted that the distribution contracts de facto excluded sale of the PFDC products via the internet.

In its judgment, on a preliminary reference from the Paris Court of Appeal the CJEU held that article 101(1) TFEU must be interpreted as meaning that (in the context of a selective distribution system) a contractual clause resulting in a ban on the use of the internet for sales amounts to a by-object restriction on competition where:

> *following an individual and specific examination of the content and objective of that contractual clause and the legal and economic context of which it forms a part, it is apparent that, having regard to the properties of the products at issue, that clause is not objectively justified.*[51]

Coty

Coty is a more recent case,[52] concerning a manufacturer of luxury cosmetics that banned its selected distributors from using third-party online marketplaces such as Amazon. Unlike the total sales ban in *Pierre Fabre*, the internet sales restriction in *Coty* was not absolute since authorised distributors were permitted to sell online via their own websites.

Apart from requirements that a bricks-and-mortar sales location must highlight and promote the luxury character of Coty brands,[53] the contractual framework linking the parties included a supplemental agreement on internet sales, which provided, in clause 1(3), that 'the authorised retailer is not permitted to use a different name or to engage a third-party undertaking which has not been authorised.'

In March 2012, Coty Germany revised both the selective distribution network contracts and the supplemental agreement on internet sales. It provided in clause I(1) of the supplemental agreement that:

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51 *Pierre Fabre* op cit, paragraph 47 of the judgment. In effect, the CJEU decided that the presence and advice of a registered pharmacist was not required for purchases of cosmetic products.

52 *Coty Germany*, judgment of 6 December 2017, op cit, published in the electronic Reports of Cases (Court Reports – general).

53 Article 2(1)(3) of the distribution contract required that 'the décor and furnishing of the sales location, the selection of goods, advertising and the sales presentation must highlight and promote the luxury character of Coty Prestige's brands.'

> *the authorised retailer is entitled to offer and sell the products on the internet, provided, however, that [such] internet sales activity is conducted through an 'electronic shop window' of the authorised store and the luxury character of the products is preserved.*

Further, clause I(1)(3) of that supplemental agreement expressly prohibited the use of a different business name or the recognisable engagement of a third-party undertaking that was not an authorised retailer of Coty Prestige. A footnote to that clause stated that:

> *accordingly, the authorised retailer is prohibited from collaborating with third parties if such collaboration is directed at the operation of the website and is effected in a manner that is discernible to the public.*

Coty's long-time distributor, Parfümerie Akzente, refused to approve the proposed amendments to the distribution contract, and Coty Germany brought an action before a national court of first instance seeking an order prohibiting the distribution of products bearing the brand at issue via the platform amazon.de, in application of clause I(1)(3).

In its judgment, on a preliminary reference from the Oberlandesgericht Frankfurt am Main, the CJEU addressed the lawfulness of the specific clause prohibiting the use of third-party online marketplaces. It first clarified that a specific contractual clause designed to preserve the luxury image of goods will be lawful under article 101(1) TFEU provided it is proportionate to the objective pursued.[54,55]

The Court of Justice went on to analyse whether the restriction on third-party online marketplaces was proportionate. It indicated in paragraphs 55–57 that such restrictions were likely to be proportionate to the aim of preserving the luxury image of the products in question.

With regard to the latter point, it is particularly helpful to also take account of Advocate General Wahl's opinion in *Coty*.[56] Advocate General Wahl had also concluded that the prohibition on online marketplaces was likely to be proportionate and contrasted that situation with the contract arrangements in *Pierre Fabre*.

In his view the prohibition on authorised distributors making use of third-party online platforms may be excluded from the scope of article 101(1) TFEU:

> *in that it is likely to improve competition based on qualitative criteria. By expanding on the considerations hitherto applied in relation to selective distribution, that prohibition is likely to improve the luxury image of the products concerned in various respects: not only does it ensure that those*

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54 'Article 101(1) TFEU must be interpreted as meaning that a selective distribution system for luxury goods designed, primarily, to preserve the luxury image of those goods complies with that provision to the extent that resellers are chosen on the basis of objective criteria of a qualitative nature that are laid down uniformly for all potential resellers and applied in a non-discriminatory fashion and that the criteria laid down do not go beyond what is necessary.' *Coty*, op cit, paragraph 36 of the judgment.

55 '. . . such a [selective distribution] system, . . . is lawful under Article 101(1) TFEU provided that the criteria mentioned in paragraph 36 of the present judgment are met.' *Coty*, op cit, paragraph 40 of the judgment.

56 ECLI:EU:C:2017:603, Opinion of 26 July 2017.

> *products are sold in an environment that meets the qualitative requirements imposed by the head of the distribution network, but it also makes it possible to guard against the phenomena of parasitism, by ensuring that the investments and efforts made by the supplier and by other authorised distributors to improve the quality and image of the products concerned do not benefit other undertakings.*
>
> *That prohibition is clearly distinguished from the clause at issue in* [Pierre Fabre].[57]

After contrasting that situation with the absolute ban on internet sales resulting from the contract terms in *Pierre Fabre*,[58] he continued:

> *The clause at issue in the main proceedings still allows authorised distributors to distribute the contract products via their own internet sites. Likewise, it does not prohibit those distributors from making use of third-party platforms in a non-discernible manner in order to distribute those products.*
>
> *As the Commission has observed, relying in particular on the results of its sector inquiry, it is apparent that, at this stage of the development of e-commerce, distributors' own online stores are the preferred distribution channel for distribution via the internet. Thus, notwithstanding the increasing significance of third-party platforms in the marketing of retailers' products, the fact that authorised distributors are prohibited from making use in a discernible manner of those platforms cannot, in the present state of development of e-commerce, be assimilated to an outright ban on or a substantial restriction of internet sales.*[59]

Guess

The Commission opened an antitrust investigation into the selective distribution agreements and practices of Guess,[60] the clothing manufacturer, in June 2017. The antitrust investigations led to the conclusions that Guess's distribution agreements restricted authorised retailers from:

- using the Guess brand names and trademarks for the purposes of online search advertising;
- selling online without a prior specific authorisation by Guess;
- selling to consumers located outside the authorised retailers' allocated territories;
- cross-selling among authorised wholesalers and retailers; and
- independently deciding on the retail price at which they sold Guess products.'[61]

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57 Opinion of AG Wahl, Coty, op cit, at paragraphs 106 and 107.

58 In paragraphs 108 and 109 AG Wahl continued: 'It will be recalled that, in the judgment in *Pierre Fabre Dermo-Cosmétique*, the Court ruled that the clause in a contract that absolutely prohibited authorised distributors from selling the contract products online could constitute a restriction by object and therefore be contrary to article 101(1) TFEU . . . In the present case, it must be emphasised that, far from imposing an absolute prohibition on online sales, Coty Germany only required its authorised distributors not to sell the contract products via third-party platforms, since, according to the network head, such platforms are not required to comply with the qualitative requirements which it imposes on its authorised distributors.'

59 Opinion of AG Wahl, *Coty*, op cit, at paragraphs 110 and 111.

60 *Guess*, Case AT.40428 Guess, available at: https://ec.europa.eu/competition/antitrust/cases/dec_docs/40428/40428_1205_3.pdf.

61 See Commission Press Release: 'Antitrust: Commission fines Guess 40 million euro for anticompetitive agreements to block cross-border sales' of 17 December 2018 available at: https://ec.europa.eu/commission/presscorner/detail/en/IP_18_6844, visited on 24 January 2020.

The restrictive provisions and practices implemented by Guess formed part of an overall company strategy that aimed to divert online sales of Guess products towards Guess's own website and restrict intra-brand competition among authorised distributors. At paragraph 138 of its decision the Commission said:

> *By means of the contractual provisions and practices referred to [. . .], Guess Europe effectively restricted intra-brand competition and partitioned national markets for its products contrary to Article 101(1) of the Treaty. There are no circumstances in the economic or legal context of those provisions and practices to support a finding that they were not liable to impair competition or did not have an anticompetitive object within the meaning of Article 101(1) of the Treaty.*

The Commission found that by restricting its own retailers from online advertising and selling cross-border to consumers in other member states (geo-blocking), for the purpose of protecting sales through its proprietary website, Guess intentionally committed (by object) infringements of EU competition rules. The fine imposed was reduced by 50 per cent to just under €40 million to take account of the fact that Guess had cooperated with the Commission beyond its legal obligation to do so.

Ping Europe Ltd: a national decision invoking the EU jurisprudence [62]

In August 2017, the United Kingdom's Competition and Markets Authority (CMA) issued a decision fining Ping Europe Ltd for a ban on its approved retailers selling its products over the internet. In the decision, the CMA found that Ping, a manufacturer of golf clubs, golf accessories and clothing, had infringed the prohibition in Chapter I of the UK Competition Act 1998 and article 101 TFEU against restrictive agreements by entering into agreements with two UK retailers containing clauses prohibiting those retailers from selling Ping golf clubs online.

The decision found that those agreements restricted competition by object and did not benefit from any exclusion or exemption. It directed Ping to bring the alleged infringements to an end and imposed a fine of £1.45 million. Ping filed a notice of appeal on 25 October 2017 contesting both the finding of infringement and the imposition and amount of the penalty. In summary, the

62 The UK is no longer a member state of the EU as of 1 February 2020. The transitional period, agreed as part of the Withdrawal Agreement, expired on 31 December 2020. On 24 December 2020, agreement on a UK–EU Trade and Co-operation was announced. The British Prime Minister, Boris Johnson, confirmed: 'This Agreement with the European Union is designed to honour the instruction of the British people – expressed in the referendum of 2016 and the general election last year – to take back control of our laws, borders, money, trade and fisheries. It changes the basis of our relationship with our European neighbours from EU law to free trade and friendly cooperation'. (Emphasis added) Foreword from the UK Government Summary Explainer updated 2 February 2021, available from www.gov.uk/government/publications/agreements-reached-between-the-united-kingdom-of-great-britain-and-northern-ireland-and-the-european-union/summary-explainer.

UK Competition Appeals Tribunal upheld the CMA's finding that Ping's contract terms were an infringement of the Chapter I prohibition of the UK Competition Act and article 101 TFEU by object.[63]

Social media

Social commerce

Social commerce, a subset of e-commerce, can be defined as the delivery of e-commerce activities and transactions via the social media environment (mostly on social networks and by using participative software). Joining a blog or discussion group on a brand-related topic in which likes, dislikes, opinions and activities are shared, would be included in social commerce. However, notwithstanding the popularity of social media itself, and with the exception of the endorsement activities of certain online personalities, few social commerce vendors have so far achieved prominence.

Factors that affect social commerce

A recent article for the Journal of Retailing and Consumer Services investigated various factors that influence social commerce on Instagram.[64] Their results confirmed (among other things) the positive effects on social commerce of trust, user habits and perceived ease of use. In business terms, their conclusions indicated that social commerce vendors should understand and be attentive to the specificity of the social commerce platform in question:

> *Instagram is built on the principle of sharing pictures and videos with friends or, as the company would call it on its official website, . . . 'we're building Instagram to allow you to experience moments in your friends' lives through pictures as they happen' (Instagram Team, 2015). Compared to other social media platforms, Instagram is mainly focused on the ease and simplicity of sharing visual media from smartphones. Firms are not expected to interact with users on Instagram. However, they may share images and videos about their offerings, which fits to the platform usage; and they may foster social interactions between users.*[65]

Although the research focused on Instagram, the business conclusions would seem broadly applicable to other social media sites such as Facebook, MySpace, Twitter or LinkedIn.

Potential drawbacks of social commerce – a note of caution

The recent article 'Social media revenge: A typology of online consumer revenge' provides an analysis of the potential drawbacks of social commerce.[66] The managerial implications include that companies can generally prevent revenge actions (by which angry customers strike back at

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63 www.catribunal.org.uk/judgments/127911217-ping-europe-limited-v-competition-and-markets-authority-judgment-2018-cat-13-7. Judgment of 7 September 2018. For a helpful survey of national cases concerning restrictions of on-line sales imposed by suppliers, see 'Vertical Restraints in On-line Sales: Comments on Some Recent Developments,' Josefine Hederström and Luc Peeperkorn, *Journal of European Competition Law & Practice*, 2016, Vol 7, No. 1 in part IV A, pages 18–20.

64 Investigating the drivers for social commerce in social media platforms: Importance of trust, social support and the platform perceived usage, *Journal of Retailing and Consumer Services* 41 (2018) pages 11–19, IB Yahia et al.

65 IB Yahia et al, op cit, page 17.

66 *Journal of Retailing and Consumer Services* 45 (2018) 239–255, ZM Obeidat et al.

firms that they feel have wronged them) on social media by offering quick and suitable recovery actions as soon as a customer makes a complaint.[67]

Conclusions and practical suggestions for franchise networks

Challenges for franchisors and franchisees

The challenges raised above essentially concern three different problems, namely:

- encroachment (both by the franchisor on its franchisees' sales and by franchisees outside their allocated territories);[68]
- free-riding (or what Advocate General Wahl referred to as 'parasitism' in his *Coty* opinion[69]); and
- the franchisor's ability to exercise a measure of control over its franchisees' websites.[70]

Problems tend to surface when agreements are renewed or general terms and conditions are changed. The implementation of e-commerce in the franchising network is a real challenge for the commercial relations between the franchisor and its franchisees. Factors that may affect the extent to which franchisees are willing to accept new contract terms for the e-commerce channel include the scale and the age of the franchise network (an objective factor) and the level of trust in the franchisor (a subjective factor).[71]

Multi-channel sales and the e-commerce environment

Clearly the political and legislative initiatives being taken now are intended to facilitate the development of cross-border e-commerce within the EU in the future. These are not necessarily developments that will affect all franchise networks, many of which will have an essentially local customer base, but they do provide both opportunities and threats for franchises based on products or services capable of being marketed and distributed across borders.

Application of the VBER, the CGVR and the CJEU case law

It is clear from the VBER and the explanations provided in the CGVR that the broad assumption of EU competition law (which is largely mirrored by individual member states' competition laws, but without the requirement that there shall be an effect on trade between member states) is

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67 The researchers also noted that several respondents indicated that their motivation for online revenge was due to changes made to their original contracts. They therefore suggested that firms should highlight their customer service procedures and policies more explicitly at the start of any customer interaction. ZM Obeidat et al, op cit, page 251.

68 For an historical account of encroachment in the United States see Franchise Encroachment, Robert W Emerson, *American Business Law Journal* Volume 47, Issue 2, 191–290, Summer 2010.

69 Other terms for types of free-riding include: showrooming or ROBO (research offline and buy online) and webrooming (meaning research online and purchase offline).

70 For the importance of preserving the uniformity of the franchise concept and the brand see Franchise et strategies multi-canal, Gérard Cliquet, November 2011 at pages 12–13 available from: https://innovation-regulation.telecom-paris.fr/wp-content/uploads/2017/11/009-Papier-Franchise-et-multicanal-Gérard-Cliquet.pdf?lang=fr, visited on 31 January 2021.

71 On this point, see further: 'Le commerce et les réseaux de franchise, ouvrage collectif', R Balmann, et al, October 2012, at 2.1.2 Les réseaux de franchise et la stratégie multi canaux, pages 50–51.

that franchisees shall be given access to the internet as a marketing channel. Nevertheless, the case law indicates that such access may be subjected to certain qualitative requirements.

The business format franchise certainly has characteristics that are very similar to selective distribution in respect of maintaining the quality and prestige of the business offering. As Advocate General Wahl explained in *Coty*: 'at this stage of the development of e-commerce, distributors' own online stores are the preferred distribution channel for distribution via the internet'. However, that does not in itself solve the issue of whether individual franchisees or the franchisor should operate the website.

Rather than adopt the *Coty* approach (of authorising the franchisee's internet sales provided they are made through a recognisable franchise 'shop window'), certain franchisors may decide to take on the responsibility for organising internet sales and marketing centrally.[72] If they do so, they will need to respect the contracts with and the autonomy of the franchisees, have regard to the balance between online and bricks-and-mortar sales, while also respecting the CGVR guidance.[73] This may require substantial investment in state-of-the-art online platforms to stimulate franchisee usage. There will therefore need to be agreement on an acceptable sharing of both the costs (investments) and the benefits, which recognises the importance of maintaining commercial relations based on mutual trust and cooperation.[74]

Each franchisor must set up a system to address the issue of e-commerce and develop policies and procedures most effective for their specific franchise that will adequately address and take care of the needs and objectives of both parties.[75]

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72 In certain cases, for example, online dating, it should also be recognised that the business software to enable internet marketing can itself be an essential element of the franchise format.

73 It will be recalled that examples of hard-core restrictions of internet usage referred to in CGVR paragraph 52 include: '(c) an agreement that the distributor shall limit its proportion of overall sales made over the internet. . . . (d) an agreement that the distributor shall pay a higher price for products intended to be resold by the distributor online than for products intended to be resold offline. This does not exclude the supplier agreeing with the buyer a fixed fee (that is, not a variable fee where the sum increases with the realised offline turnover as this would amount indirectly to dual pricing) to support the latter's offline or online sales efforts.'

74 A general principle of good faith (derived from Roman law) is recognised by most civil law systems – including those of Germany, France and Italy. The Belgian Civil Code, article 1134 explicitly mentions the role of good faith in the execution of contracts. The principle is also recognised (although with certain limitations) in common law jurisdictions. For example, although perhaps formally based on the equitable doctrine of estoppel, the decision in *Dymocks* may be read as an expression of such a principle. See in particular the cases on good faith referred to at paragraph 16 of the judgment of the Chief Justice in *Equity Hodgson: Muschinski v Dodds* (1985) 160 CLR 583 at 613, 619–620; *Alcatel Australia Ltd v Scarcella* (1998) 44 NSWLR 349 at 363–9; and *Stern v McArther* (1988) 165 CLR 489.) In England and Wales, see *Yam Seng Pte Ltd v International Trade Corporation Ltd* [2013] EWHC 111 QB at paragraph 124 of the judgment of Mr Justice Legatt.

75 See 'Encroachment: legal restrictions on retail franchise expansion', W Slater Vincent, 1998 *Journal of Business Venturing* 13, pages 29–41, which addresses questions of physical or spatial encroachment on the franchise territory.

Evaluation of the VBER and public consultation

In the meantime, the VBER is set to expire on 31 May 2022 and the EU Commission has started a process of evaluation to check whether the Regulation is still 'effective, efficient, relevant, in line with other EU legislation and adds value'. A public consultation was launched on 18 December 2020 lasting until 26 March 2021.[76] To the extent that franchise networks and the European franchise associations feel the rules affecting franchises need to be changed or clarified, there is an opportunity to put those views forward.

76 https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12636-Revision-of-the-Vertical-Block-Exemption-Regulation/public-consultation; see also the Commission Staff Working Document, 'Evaluation of the Vertical Block Exemption Regulation', 8 September 2020 SWD (2020) 172 final, available at: https://ec.europa.eu/competition/consultations/2018_vber/staff_working_document.pdf, visited on 31 January 2021.

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