



DIRECTORATE-GENERAL FOR INTERNAL POLICIES

POLICY DEPARTMENT  
ECONOMIC AND SCIENTIFIC POLICY **A**



Discrimination of Consumers in the Digital Single Market

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Consumer Protection**

# Discrimination of Consumers in the Digital Single Market

STUDY





**DIRECTORATE GENERAL FOR INTERNAL POLICIES**  
**POLICY DEPARTMENT A: ECONOMIC AND SCIENTIFIC POLICY**

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## **STUDY**

### **Abstract**

The study collates information on discrimination against consumers on grounds of place of residence or nationality in the Digital Single Market (DSM). Collected evidence indicates such practices as refusals to sell or discriminatory conditions depriving consumers of access to goods and services on DSM or obliging consumers to pay higher prices. The study assesses discrimination from the perspective of different areas of European law including Article 20 (2) of Services Directive, Private International Law, Competition Law and Intellectual Property Law, and provides for policy recommendations.

This document was requested by the European Parliament's Committee on Internal Market and Consumer Protection (IMCO).

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## LIST OF ABBREVIATIONS

<b>ADR</b>	Alternative Dispute Resolution
<b>Art.</b>	Article
<b>BATNA</b>	Best alternative to negotiated agreement
<b>BER</b>	Block Exemptions Regulations
<b>CRM</b>	Customer Relationship Management
<b>DSM</b>	Digital Single Market
<b>EESC</b>	European Economic and Social Committee
<b>EU</b>	European Union
<b>IP</b>	Intellectual Property
<b>IPR</b>	Intellectual Property Rights
<b>MIF</b>	Multilateral Interchange Fees
<b>ODR</b>	Online Dispute Resolution
<b>Para.</b>	Paragraph
<b>PCW</b>	Price Comparison Websites
<b>SEPA</b>	Single Euro Payments Area
<b>SME</b>	Small and Medium Enterprises
<b>TEC</b>	Treaty on the European Community
<b>TFEU</b>	Treaty on the Functioning of the European Union
<b>TTBER</b>	Technology Transfer Block Exemption Regulation
<b>WATNA</b>	Worst alternative to negotiated agreement



## EXECUTIVE SUMMARY

### Obstacles hindering consumers participation on the DSM

**33.2 % of consumers from across the EU confirmed purchasing goods and services via the Internet from sellers located in their country and only 7.4 % of Internet purchases are of a cross-border dimension<sup>1</sup>.** The level of consumers' participation in DSM may be a cause for concern.

E-commerce, in particular the DSM, has an enormous potential for further development of the internal market. E-consumers may benefit from DSM through wider choice of goods and services, more competitive offers, more attractive prices and more flexible contractual terms and conditions. Since e-shops are accessible everywhere and greatly facilitate the comparison of prices, consumers may increasingly order services internationally by making use of the internal market.

However, it is becoming increasingly noticeable that businesses, in particular service providers, often restrict their activities to a certain country or a certain group of countries. The practice of businesses to limit their activities to certain states or regions creates frustration on the part of consumers, who feel that they are excluded from the internal market. Such practices decrease consumers' confidence and, finally, the level of consumers' contribution to the market.

**In the DSM, a new set of obstacles have also arisen which were unknown to the world of physical sales.**

Whether of a legal or factual nature, national or private character, whether imposed at the level of retail or supply, or whether aiming to distinguish consumers' groups or territories, the obstacles of the DSM, frustrate and discourage consumers active in the DSM.

**The diversity of sources and the variable legal nature of DSM obstacles require a broad interdisciplinary approach to be adopted for the subject of consumer discrimination in the DSM.** This study aims to analyse various aspects of, and grounds for, consumer discrimination from the different perspective of private international law (Brussels I and Rome I), freedom of goods and services (Services Directive), competition law and intellectual property law.

### Evidence of practices discriminating consumers on the DSM

Price level and wider choice of products or services are important factors for consumers' decision-making.

**56 % of consumers ordered goods or services cross-border because the particular product in question could not be sourced in the national market.** In some Member States there are products for which consumers cannot find online domestic offers at all<sup>2</sup>.

**For 65 % of consumers a reason for buying cross-border were cheaper prices.** In 13 of 27 Member States<sup>3</sup> a number of shoppers were instructed to search for a list of 100 popular products on the internet and to compare international offers with their local prices. The shoppers were able to find a cross-border offer that was at least 10 % cheaper than

<sup>1</sup> Flash Eurobarometer 299, p.80. Compare data cited in chapter 1.1. of this study.

<sup>2</sup> Shoppers in Cyprus, Malta, Luxembourg, Lithuania, Latvia, Ireland, Belgium, Estonia, Portugal and Finland could not find domestic online offers for at least half of the products they were searching for. See: Mystery shopping evaluation of cross-border e-commerce in the EU, data collected on behalf of the European Commission (2009), p. 37 f. The summary of the main findings of the study is also reported in: Communication on e-commerce, COM(2009) 557 final.

<sup>3</sup> Portugal, Italy, Slovenia, Spain, Denmark, Romania, Latvia, Greece, Estonia, Finland, Hungary, Cyprus, Malta.

the best domestic offer (all costs, including shipping, included) for at least half of all the product searches<sup>4</sup>. These facts demonstrate that the DSM could potentially be very beneficial for consumers, but in numerous cases they are not able to take advantage of the potential of cross-border online shopping.

E-commerce is a vital key in facilitating consumers' purchasing cross-border. Despite this, consumers purchasing products unavailable on their national market are still faced with obstacles causing their frustration and disappointment. However, on average, **only 39 % cross border orders consumers are not refused at some point in the process of placing an order**<sup>5</sup>. There is rising frustration among consumers, particularly residents of smaller Member States, who are not allowed to buy products from other Member States, or are allowed to purchase on-line but on less attractive terms due to their place of residence. **A refusal to sell to foreign consumers prevents the emergence of a true single market for e-commerce.**

There are three common types of market practices - which are detrimental from the consumers' perspective - which differentiate between different consumers using the DSM: **simple refusal to sell, automatic re-routing, and unjustified diversifying of sale conditions.**

Several marketing strategies constitute refusals to sell. Firstly, e-shops may simply refuse to allow consumers with IP-addresses from certain countries to purchase online. This refusal to sell usually takes place at one of the stages in placing an order. Very often the consumer realises only when attempting to place an order that it is impossible. Different forms of **discrimination by refusing to sell** may affect a consumer who is searching for a specific product. Such practices consist in offering consumers - residents of one Member State a **completely different selection of products** than offered in another Member State. Consumers are often redirected from a chosen, foreign e-shop to a satellite e-shop placed in Member State of their place of residence, where only goods of a certain selection are on sale.

Secondly, service providers use automatic relocation and direct the consumer to another e-shop, usually a satellite e-shop, without the consumer's consent or knowledge. These practices cause consumer frustration, the impression of being excluded from the internal market, or even being discriminated against on the basis of their country of residence.

The third strategy consists of accepting orders from consumers of particular group or country of residence on different terms and conditions. A very frequent sub-type relates to inflated delivery costs, which are often significantly higher for consumers ordering from abroad. In the context of discriminatory practices, two types of contracts must be distinguished: contracts dealing with physical goods and those over digital content (e.g. music, video downloads or apps). As for contracts for digital content, the traditional, objective reasons for increased prices, such as higher delivery costs, do not exist. There are, however, specific legal problems related to digital content, such as issues of intellectual property, which limit their availability and allow for market compartmentalisation.

Notwithstanding the intangible **dimension of digital content**, their transferability, multiplicability or lack of durability, makes digital content different from tangible goods offered through traditional sales to consumers. Consumers are often interested only in data transfer, instead of purchasing durable data carriers with digital content. European

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<sup>4</sup> Mystery shopping evaluation (2009), p. 39 ff.

<sup>5</sup> Mystery shopping evaluation (2009), p. 39 ff.

legislation has not created the typologically coherent legal framework suited to digital content. The European Commission Project for a Regulation on Common European Sales Law<sup>6</sup> subjects digital commercial transactions to the sometimes inadequate structure of sales contract. The special nature of digital content makes its sale clearly distinguishable from the cross-border sale of tangible goods. The intangible character of digital content seems to make the purchasing of digital products closer to the supply of services.

Whether practices which differentiate between certain goods or services or types of consumers may be justified must be assessed on a case by case basis. One practice with a significant impact on the DSM which distinguishes between consumers is limiting the proper use of digital content to a geographically restricted area. Providers do usually offer to transfer the digital content to another country, but this often requires completing a rather cumbersome online request.

Technological development enables more advanced mechanisms of consumer discrimination (e.g. exclusion by means of extensive collecting and analysing of consumer data). It is, however, extremely difficult to predicate future technological creations, inventions and ways of exploiting them by certain businesses to the detriment of consumers.

If one compares the situation within the DSM with the retail conditions on business premises, the consumer who tries to conclude a contract on business premises is rarely frustrated, whereas this seems often to be the case when online shops are used.

### **Comprehensive cross-field line of removing obstacles**

Despite the existing EU legislation facilitating consumers' participation in the DSM, as well as a generally high level of approximation of provisions protecting consumers on a national level, consumers purchasing on the DSM are still discriminated against. **Improving the consumers' position in the digital market requires a comprehensive multi-disciplinary approach and coherent measures taken in numerous fields of the European legislation.**

The **anti-racism provisions** of the Treaty and of secondary law are usually not infringed by a service provider's refusal to accept orders of consumers from other Member States. The legal interest of customers, including consumers, which is infringed by such practices is usually not their dignity; it is simply their right to participate in the internal market. Only in exceptional cases, where refusal to sell infringes the dignity of consumers is it possible for the provisions of the Treaty and of secondary law against discrimination on grounds of race and ethnic origin to have been infringed. This is the usually the case where a service provider generally refuses to accept orders from nationals of a certain state (irrespective where they are resident). Such arbitrary discrimination displays contempt for the citizens of a certain state on the mere ground that they are citizens of that state and is therefore prohibited.

**Article 18 of the Treaty on the functioning of the European Union (TFEU)** explicitly contains a directly applicable, autonomous, absolute and general prohibition of discrimination on grounds of nationality and in paragraph (2) a power allowing for the introduction of further specific prohibitions of discrimination. Article 18 TFEU is undoubtedly directly applicable against the Member States and the EU itself. The ECJ has carefully extended the direct applicability of several of the fundamental freedoms to private entities. It remains to be seen whether this line of jurisprudence will also be extended to individual service providers in the DSM. Such an extension would have to be balanced against the fundamental rights of the businesses concerned and would therefore only be feasible in

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<sup>6</sup> COM (2011) 635 final.

cases where improvements in the functioning of the internal market outweigh the fundamental rights of the affected businesses.

The **fundamental freedoms** of the Treaty usually do not defend customers against discriminatory practices of service providers in the DSM. Their purpose is usually not to force market participants to use this freedom fully. The fundamental freedoms usually do not protect one market participant (here: the customer) from another (here: the business which refuses to sell or only sells on less favourable terms). The few exceptions presently formulated by the ECJ concern powerful associations or trade unions, perhaps also individual employers, but not service providers in the DSM. However, the fundamental freedoms constitute an important element when balancing different objectives of EU law, such as e.g. the freedom of businesses to choose whom to do business with or the protection of intellectual property.

Article 20 (2) of the **Services Directive** is the most prominent piece of legislation against discrimination in the single market. This provision prohibits general conditions of access to a service, containing discriminatory provisions relating to the nationality or place of residence of the recipient. It is, however, severely misconceived. Nearly every aspect of the provision is entirely unclear. It is already questionable whether it is applicable merely to services in a narrow sense or also to the sale of goods. It is furthermore unclear whether this provision simply protects natural persons or also legal persons. It is, moreover, entirely unclear what constitutes a direct justification by objective criteria, which allows for differences in the conditions of access. This also seems to be the reason why there is presently no discernible enforcement activity throughout Europe. It needs to be considered whether the whole Article should be repealed – and not replaced by another potentially oppressive rule, but by further unification of the national laws, diminishing some of the actual obstacles to cross-border commerce in the DSM.

The **Common European Sales Law** and recent **ADR/ODR legislation** are steps in the right direction of removing the obstacles of the DSM instead of putting pressure on businesses to extend their activities to the whole territory of the EU.

The current system of **international private and procedural law** of the EU may, particularly in consumer cases, force the business to litigate abroad and to apply foreign consumer law which is unknown to the business. This possibility of litigation in foreign courts and the differences in the laws applicable to the contract might be used by businesses as a ground to refrain from concluding contracts with customers from another Member State. In the long run, the development of optional instruments, such as the Common European Sales Law, and of trustworthy ODR schemes may help in overcoming this justification. The current state of the available ODR schemes, however, is far from satisfactory in this regard.

### Assumptions and measures against consumers' discrimination

**Enhancement of e-commerce depends on the safety and predictability of the legal framework.** It seems that the most effective strategy to build such an environment for e-commerce would be to **create incentives and unleash market forces**.

**Concrete policy recommendations** for the European Union could include:

- (1) Removing discernible and surmountable reasons for not making use of the internal market, which includes removing differences of the applicable law by harmonisation, by introducing optional instruments (such as the Common European Sales Law) and by supporting trustworthy ODR schemes.
- (2) More rigorously enforcing proceedings under competition law against businesses which have a dominant market position or create agreements discriminating

consumers or abusing legally allowed exemptions from restrictions of Article 101 (1) of the TFEU.

- (3) More rigorously enforcing proceedings under competition law against agreements and concerted practices which have as their object to hinder retail traders from accepting orders from consumers who actively make use of the DSM by shopping across borders between Member States (i.e. "passive sales").
- (4) Limiting geographically restricted licences that divide the internal market and approximating national IP legislation to create a unified framework of EU IP law.
- (5) Educating consumers and raising their awareness of practices impeding the exercise of their freedoms.
- (6) Creating an easily accessible website where customers can complain when discriminated against.
- (7) Making such complaints public when justified.
- (8) Obliging all e-shops to disclose their internal market policy prominently, in particular including those countries from which they accept orders and whether there are different conditions for certain countries.
- (9) Monitoring activities of European institutions which publicly provide examples of best and worst practice in order to make businesses rethink their strategies.

# 1. CONSUMER DISCRIMINATION IN DSM

## KEY FINDINGS

- Market studies highlight the importance of the Internal Market for consumers and the contribution which consumers make to further development of the Internal Market.
- **56 % of consumers ordered goods or services cross-border because the particular product in question could not be sourced in the national market.**
- For **65 % of consumers one reason for buying cross-border was cheaper prices.**
- E-commerce is a vital key in facilitating consumers' purchasing cross-border. Despite this, consumers who purchase products unavailable on their national market are still faced with obstacles causing frustration and disappointment. However, on average, **only 39 % cross border orders consumers are not refused at some point in the process of placing an order.** There is rising frustration among consumers, particularly residents of smaller Member States, who are not allowed to buy products from other Member States, or are allowed to purchase on-line but on less attractive terms due to their place of residence. **A refusal to sell to foreign consumers prevents the emergence of a true single market for e-commerce.**
- There are three common types of market practices which differentiate between different consumers using the DSM: simple refusal to sell, automatic re-routing, and unjustified diversifying of sale conditions. Several marketing strategies constitute refusals to sell. Firstly, e-shops may simply refuse to allow consumers with IP-addresses from certain countries to purchase online. This refusal to sell usually takes place at one of the stages in placing an order. Very often the consumer realises only when attempting to place an order that it is impossible. Secondly, service providers use automatic relocation and direct the consumer to another e-shop, usually a satellite e-shop, without the consumer's consent or knowledge. These practices cause consumer frustration, the impression of being excluded from the internal market, or even being discriminated against on the basis of their country of residence. The third strategy consists of accepting orders from consumers of particular group or country of residence on different terms and conditions. A very frequent sub-type relates to inflated delivery costs, which are often significantly higher for consumers ordering from abroad.
- Technological development enables more advanced mechanisms of consumer discrimination (e.g. exclusion by means of extensive collecting and analysing of consumer data). It is, however, extremely difficult to predicate future technological creations, inventions and ways of exploiting them by certain businesses to the detriment of consumers.
- In the context of discriminatory practices, two types of contracts must be distinguished: contracts dealing with physical goods and those over digital content (e.g. music, video downloads or apps). As for contracts for digital content, the traditional, objective reasons for increased prices, such as higher delivery costs, do not exist. There are, however, specific legal problems related to digital content, such as issues of intellectual property, which limit their availability and allow for market compartmentalisation.



- Whether practices which differentiate between certain types of consumer may be justified must be assessed on a case by case basis. One of the more invasive practices which distinguishes between consumers is the restricting the proper use of digital content to a geographically restricted area. Providers do usually offer to transfer the digital content to another country, but this often requires completing a rather cumbersome online request.
- If one compares the situation within the DSM with the retail conditions on business premises, the consumer who tries to conclude a contract on business premises is rarely frustrated, whereas this seems often to be the case when online shops are used.
- Search engines, such as Google, and Price Comparison Websites (PCW) play a particularly important role with regard to the issue of discrimination against consumers from different Member States, since these sources of information are able to influence consumers' decisions to buy and most importantly from whom they buy. The default settings of search engines and PCW limit their results to offers available nationally. As a result, the consumer is not even made aware of the possibility of better offers from other Member States' online stores (cf. discrimination by way of refusal to supply). This state of affairs is also problematic for business, since the offers of businesses from Member States other than the search engine or PCW are unable to reach the greatest number of consumers in the single market. This naturally prevents the DSM from being fully exploited.

### 1.1. Extent of consumer discrimination on DSM

Between December 2010 and February 2011, 32 % of all consumers who shopped online bought from an on-line shop from another Member State<sup>7</sup>. Such e-consumers represent 9 % of the total number of consumers in the EU<sup>8</sup>.

65 % of consumers bought cross-border because of lower prices<sup>9</sup>.

**For 56 % of consumers one reason for buying cross-border is that the particular product in question could not be sourced on the national market<sup>10</sup>.**

The "Mystery Shopping Evaluation of Cross-Border E-Commerce in the EU"<sup>11</sup> showed that, on average, it was only possible in 39 % of cases to place a cross border order without being refused at some point in the process of placing an order. The study revealed that in some Member States there are many products for which consumers cannot find online domestic offers<sup>12</sup>. Shoppers in Cyprus, Malta, Luxembourg, Lithuania, Latvia, Ireland, Belgium, Estonia, Portugal and Finland could not find domestic online offers for at least half of the products they were searching for.

<sup>7</sup> Consumer market study on the functioning of e-commerce and Internet marketing and selling techniques in the retail of goods (2011), p. 32 f.

<sup>8</sup> Eurostat, Information society statistics (2010), data extracted on 14 April 2010.

<sup>9</sup> Consumer market study (2011), p. 38 f.

<sup>10</sup> Consumer market study (2011), p. 38 f.

<sup>11</sup> Mystery shopping evaluation of cross-border e-commerce in the EU, data collected on behalf of the European Commission (2009). The Study was conducted using the method of "mystery shoppers" whereby consumers are trained and briefed to test the market by acting as though they were going to make a purchase. These mystery shoppers shopped at online shops in all 27 EU Member States. In total, 10 964 cross-border tests were carried out. The summary of the main findings of the study is also reported in: Communication on e-commerce, COM(2009) 557 final.

<sup>12</sup> Mystery shopping evaluation (2009), p. 37 f.

These findings reveal the importance of creating a true Single Market for e-commerce. **Consumers who cannot source products on their own national online shops seek to take advantage of the Single Market through international e-shops. However, in a significant number of cases, the online retailers in other Member States refuse to sell in different ways** (and discriminate against the foreign consumer). As a result, EU citizens who wish to spend money are unable to conclude contracts within the EU. This state of affairs is yet more problematic for the European Single Market, if the consumer can buy the product outside the EU. In such a case the potential benefits of the DSM are not only unexploited, but even completely wasted<sup>13</sup>.

The same Mystery shoppers were instructed to search for a list of 100 popular products on the internet and to compare international offers with their local prices. In 13 of 27 Member States (Portugal, Italy, Slovenia, Spain, Denmark, Romania, Latvia, Greece, Estonia, Finland, Hungary, Cyprus, Malta) shoppers were able to find a cross-border offer that was at least 10 % cheaper than the best domestic offer (all costs, including shipping, included) for at least half of all the product searches<sup>14</sup>.

These findings show that the DSM could potentially be very beneficial for consumers. On the other hand, it is clear that in numerous cases consumers are not able to take advantage of the potential of cross-border online shopping. Especially in smaller Member States there is rising frustration on the part of consumers who are unable to buy products from other Member States, or who are able to do so but only on less attractive terms due to their place of residence.

Retail practices are not an exclusive source of consumer discrimination in the DSM. Technological progress may allow for less predictable, but more advanced forms and tools of discrimination on the digital environment. However, different forms of discrimination are not characteristic of, nor restricted to, cross-border transactions or the digital market. They are, in fact, general forms of discriminating against consumers.

One of the possibilities for exploiting advances in technology is the internal and external management of data relating to the business's clients, which is often related to the optimisation of the business model<sup>15</sup>. The processing of customer data is known as Customer Intelligence or, sometimes more specifically, as Customer Relationship Management (CRM). These processes collate an enormous amount of data about consumers, making it possible to create specific consumer groups and sub-groups. It is clear that the processing of such information could be used to the consumer's detriment.

The collecting of such information, such as the consumer's previous purchases, makes it much easier to price discriminate against consumers<sup>16</sup>. In connection with technological advances, businesses could use the information they collect to implement more efficiently the well-known strategies for differentiation between types of consumer. For example, the business could build consumer-groups on the basis of their place of residence (by scanning their IP addresses) and offer different prices or different terms and conditions. Through the scanning of the IP address, which is not obvious for the consumer, businesses could discriminate against consumers without their knowledge and without any public notice.

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<sup>13</sup> See also: Consumer market study (2011), p. 104 ff.

<sup>14</sup> Mystery shopping evaluation (2009), p. 39 ff.

<sup>15</sup> Customer Intelligence 2008, Status Quo und Trends im deutschsprachigen Markt, p. 4.

<sup>16</sup> L. A. Stole, Price Discrimination and Imperfect Competition, 2003, p. 29 ff.



Future technologies could also make it much easier to integrate data collected from social media with a company's business model<sup>17</sup>. The potential of such future technologies is enormous.

The areas previously mentioned are illustrative examples of ways in which the weaker position of consumers can be exploited. It is extremely difficult to predict which technological advances will be made in the future and how certain businesses will exploit them to the detriment of consumers. Extensive discussion of the means of discrimination against consumers brought about by advances in technology fall out of the scope of the present study. However, some aspects of this issue are highlighted in chapter 5 on the context Intellectual Property rights.

## 1.2. Reasons for differentiating types of consumers

### 1.2.1. Reasons given by businesses

The reasons for differences in pricing and access are, according to statements from businesses, as numerous as they are multifarious. The following reasons were given by businesses in the framework of the small scale survey carried out on business practices applying different condition of access based on the nationality or the place of residence of service recipients include<sup>18</sup>:

- direct financial costs (VAT, copyright levies in the sale of certain electronic goods);
- compliance costs (differences in implementation of the Directives);
- information and regulatory uncertainty (copyright levies, licensing in digital downloads, national implementation of the Directives);
- input from suppliers (right holders) in digital content;
- order and payment processing (address verification, payment methods, exchange rates);
- transport and delivery costs;
- customer support (language);
- corporate structure, and
- demand-side drivers, such as cultural differences or willingness to pay.

Eurobarometer indicated at the following reasons<sup>19</sup>:

- potentially higher costs due to the risk of fraud and non-payments in cross border sales compared to domestic sales (63 %);
- the perceived cost of complying with different national fiscal regulations (62 %);
- the perceived cost of complying with different national laws regulating consumer transactions (60 %);
- the perceived cost of the difficulty in resolving cross-border complaints and conflicts (59 %);
- extra costs arising from cross-border deliveries (57 %);

<sup>17</sup> A first step is the implementation of 'Facebook Connect' which allows business to connect their website with Facebook, see: <https://developers.facebook.com/docs/web/gettingstarted/>.

<sup>18</sup> Study on business practices (2009), p. 31 ff.

<sup>19</sup> Business attitudes towards cross-border sales and consumer protection, Flash Eurobarometer 224 (2008), p. 6 and 22 ff.

- the cost of ensuring an efficient after-sales service (55 %);
- costs arising from different languages (45 %).

Differences in products offered are often justified on the ground that the demand of consumers from different Member States differs and business must therefore meet different expectations and specifications with another range of products. The travel agent TUI offers, for example, completely different travel destinations for clients from Belgium and Germany<sup>20</sup>.

The legal discussion of business justifications will follow in Chapter 2.

### 1.2.2. Peculiarities of digital content

In the context of the above mentioned reasons, two types of contract can be distinguished: contracts dealing with physical goods (selling a CD/DVD) and those over digital content (downloading an e-book or music)<sup>21</sup>. The difference is important, because the market for digital goods is growing rapidly. In the United Kingdom, overall digital sales grew by 54 % in 2011 (consumer e-books sales increased by 366 %)<sup>22</sup>. Digital music revenues to record companies grew by 8 % globally in 2011 to an estimated 5.2 billion USD<sup>23</sup>.

As for digital goods/services, there are specific legal problems, such as issues of intellectual property which limit their availability. Under intellectual property law, right holders may geographically restrict licenses<sup>24</sup>. For example, it is not uncommon in this market that a seller is effectively forced to discriminate so as not to infringe the rights of other sellers. Problems could also arise where consumers buy digital content in the country of the online-shop and want to download and use the content in another country<sup>25</sup>. If the right-holder who allowed the seller to distribute the digital content prohibits delivery in another country by a clause in the distribution agreement, the source of the problem lies in the vertical agreement itself and also the proper execution of obligations under the sale contract.

For digital content, an important source of legal uncertainty for businesses relates to such licensing issues<sup>26</sup>. Licensing costs do not only involve purchasing the actual licenses. The question of with whom licensing contracts should be signed, because rights to the same content across Europe can be held by different parties<sup>27</sup>. Licences for digital content will also often involve more than one right holder<sup>28</sup>.

On the other hand, the delivery of digital goods/services is by its very nature much easier than the delivery of physical goods. Physical delivery in the traditional sense is not an issue; the product sold need only be downloaded by the consumer. As a result, the traditional justification for extra costs arising from cross-border deliveries is made irrelevant for the sale of digital content. This also applies for some problems which could arise in the delivery process (false address, damaged items, lost shipments).

Differences in the nature of the product sold are also relevant for issues of implied warranty and withdrawal. Where a physical good is defective the consumer is protected by an implied warranty and/or the right of withdrawal. Issues (and especially added costs) arising from

<sup>20</sup> Study on business practices (2009), p. 28.

<sup>21</sup> See also: Study on Digital Content Products in the EU (2012); Consumer rights in digital products (2010).

<sup>22</sup> The Publisher Association, press release Statistical Yearbook 2011, [http://www.publishers.org.uk/index.php?option=com\\_content&view=article&id=2224&Itemid=1618](http://www.publishers.org.uk/index.php?option=com_content&view=article&id=2224&Itemid=1618).

<sup>23</sup> IFPI, Digital Music Report 2012, p. 6.

<sup>24</sup> See: Chapter 5. Intellectual Property Law.

<sup>25</sup> Study on Digital Content Products in the EU (2012), p. 8 f.

<sup>26</sup> Study on business practices (2009), p. 50.

<sup>27</sup> Study on business practices (2009), p. 50.

<sup>28</sup> Study on business practices (2009), p. 53.

legal questions such as an implied warranty and the right of withdrawal could be a reason for the seller to discriminate against the consumer. As for digital goods, such problems do not arise to the same extent. A digital film or music can be played or not. Moreover, in most cases the right of withdrawal ends after the download of digital content is completed (Article 6 (3) Distance Selling Directive<sup>29</sup>). Therefore business cannot plead higher delivery costs for cross-border digital content transactions (as could be the case for physical goods) as a reason for discriminating against consumers from different Member States.

Restricting sales because of different languages is increasingly important for digital content<sup>30</sup>. Consumers may not be able to read important information on product specification and usability in a foreign language. After-sales support is also much more relevant for digital content (especially support for technical problems). If the business wants to open a shop for cross-border transactions, it has to invest in foreign-language support (and possibly in a foreign-language website). This would be a major cost driver for business<sup>31</sup>.

To summarise, although traditional justifications for discrimination used in relation to physical goods no longer apply to digital content, digital content poses different problems which may be used to discriminate against the consumer (IP rights, administrative costs of different languages). Other traditional justifications like information costs, regulatory uncertainty, the perceived cost of complying with different national fiscal regulations or potentially higher costs due to the risk of fraud and non-payments also apply to sales of digital content.

### 1.3. Types of consumer discrimination

An analysis indicates several empirical types of discriminatory practices, which consumers are faced with, and which impede the functioning of the DSM. The three common types of practice distinguishing consumers' positions in the DSM are refusal to sell, automatic re-routing and unjustified diversifying of terms of sale.

A comprehensive legal analysis of these practices follows in the remaining chapters of the study.

#### 1.3.1. Refusal to sell to consumers from other Member States

In 2010, **74 % of retailers in the EU did not sell products or services to customers in other EU countries**<sup>32</sup>. This is also the case for online-shops based in the UK. 67 % of those businesses surveyed do not target consumers resident in other Member States<sup>33</sup>. This is confirmed by the findings of the "Mystery Shopper" study since only 61 % of the attempted purchases were successful<sup>34</sup>.

Discrimination by refusal to sell or supply means that a foreign consumer cannot place an order with a specific online-shop. The consumer is prevented from placing an order because the processing of an order requires an address in a specific country. The refusal to sell may not necessarily be the result of direct action of the seller – its origin may be found further down the supply chain. For instance, a manufacturer may enforce a discriminatory practice on the distributors of its products

<sup>29</sup> Analysis of the applicable legal framework, Final Report (2011), p. 81 ff.

<sup>30</sup> See also: Ups and down(load)s - Consumer experiences of buying digital goods and services online (2010), p. 11.

<sup>31</sup> Study on business practices (2009), p. 58 f.

<sup>32</sup> Retailers' Attitudes Towards Cross-border Trade and Consumer Protection, Analytical Report, Flash Eurobarometer 300(2011), p 19 f.

<sup>33</sup> Internet shopping - An OFT market study (2007), p. 151.

<sup>34</sup> Mystery shopping evaluation (2009), p. 37 f.

A distinctive illustration of discriminatory practice is the case of a Spanish consumer, who wishes to order a product from a German online-shop. The German online-shop requires the customer to register before being able to place an order. The Spanish consumer is, however, prevented from registering because of his place of residence. The Spanish consumer is thus discriminated by refusal to sell. A notable example of an anti-competitive refusal to supply in the DSM is the abuse of dominant position considered by the Court in the Microsoft case<sup>35</sup>. The facts of the case concerned the refusal of Microsoft to provide computer protocols which would enable sellers of competing operating systems to interoperate with Microsoft Windows's operating systems and cooperate with Microsoft's clients. This practice was found to have limited the freedom of customers in choosing software provided by other operators. It was therefore considered as infringing fair competition within the EU market.

Discrimination targeting different types of consumer may result from agreements allowed under EU competition law<sup>36</sup>. Where agreements of exclusive distribution are signed, consumers resident in one Member State may experience difficulties to buy the same product from the exclusive distributor of another Member State. Many consumers have complained about this practice in relation to the sale of baby prams. Although the respective exclusive distributors are contractually bound not to sell to foreign consumers, this practice is probably in breach of competition law<sup>37</sup>. Similar restrictions arise from agreements creating selective distribution systems<sup>38</sup>. In case C-439/09 (Pierre Fabre)<sup>39</sup> a vertical agreement which created a selective distribution system provided for a contractual clause requiring that the sale of cosmetics and personal care products take place in the presence of a qualified pharmacist. The requirement excluded the sale of such products online. Accordingly, the agreement limited the cross-border online market. Competition rules allow for agreements which further vertical restrictions.

In the context of a refusal to sell, the particularities of digital content need to be taken into account<sup>40</sup>. Problems with IP rights, in particular, may be used to justify refusing to sell of digital content.

Various problems might also arise in relation to third-party rights in the sale of digital goods. Retailers might be contractually obligated to sell a product exclusively within a geographically delimited area<sup>41</sup>. Restrictions may also be allowed by rules of EU competition or IPR law<sup>42</sup>, as well as some national provisions<sup>43</sup>.

### 1.3.2. Discriminatory aspects of re-routing

The other permutation of discriminatory practices, namely re-routing, is less extreme than simply refusing to sell goods and provide services to "foreign" consumers. Instead of refusing to conclude a contract with other international consumers, the consumer is re-routed to the satellite e-shop of his or her place of residence. Country-specific websites are

<sup>35</sup> Judgment of 27.7.2012 Case T-167/08 (Microsoft) ECR (not yet published). See also: Chapter 4.5.1 of the study.

<sup>36</sup> Study on business practices (2009), p. 16.

<sup>37</sup> For a comprehensive legal analysis of such practices, see: Chapter 4. of the study (Competition law).

<sup>38</sup> See also: Chapter 4.2. of the study (Agreements infringing competition and consumers under Article 101(1) TFEU).

<sup>39</sup> Case C-439/09 (Pierre Fabre) ECR (not yet published).

<sup>40</sup> See: Chapter 1.2.2. of the study (Particularities of digital content).

<sup>41</sup> See also: Study on Digital Content Products in the EU (2012), p. 8 f.

<sup>42</sup> See: Chapter 4. and 5. of the study.

<sup>43</sup> National provisions are a result of the transposition of the Directives 2008/95 and 2001/29, see also: Chapter 5.4. of the study (Territorial restraints and national provisions).

frequently used by electronic businesses who try to adapt to the culture and particularities of the target consumers<sup>44</sup>.

The re-directing of the consumer either takes place automatically, by means of an IP-address identification check, or through a note of non-delivery to other Member States and a link to the other Member State specific e-shops<sup>45</sup>. Such a link is present either on the homepage of the e-shop or, once the consumer has undertaken the process of ordering the desired good or service, at the point when the consumer must enter his or her address. 6 % of the 10,964 cross-border transactions attempted by mystery shoppers involved this business-model<sup>46</sup>.

The re-directing mechanism is well illustrated by the example of a Polish consumer wishing to order a product from a French online-shop. The Polish consumer visits the website and tries to order the product. After the consumer has completed the ordering process and must fill in the address-field his Polish address, he is informed that he is unable to order and has to use the Polish website of the same business. An analogous example is provided by the case of purchasing digital content<sup>47</sup>. Having acquired the necessary right to sell certain tracks of music across the EU in all Member States, the music download provider divides the market geographically by creating a separate e-shop for each Member State. Each e-shop offers more or less the same music for download only at different prices. Consumers resident in another Member State wishing to order from another e-shop are automatically re-directed to the e-shop of the Member State in which they are resident.

Through the refusal to conclude contracts over the originally selected e-shop and the re-routing to another shop corresponding to that of the place of residence of the consumer, a business can avoid making cross-border sales and the associated legal and technical problems. As a result, a contract is concluded between the consumer and the relevant national subsidiary or satellite company. From a legal point of view, the originally selected business normally has no implication in the contract eventually concluded.

Following the successful re-routing of the consumer, there are several different means of discriminating against the cross-border consumer. In particular,

- different pricing (not necessarily higher);
- lesser choice<sup>48</sup>;
- or variations in quality.

Price discrimination occurs when a consumer is re-routed to the national online shop and forced to pay a higher price for the same product or service. For instance, if a consumer from Germany visits a Greek website for hotel bookings. The shop scans his IP-address and automatically redirects him to the German website of his business. On the German website, the price for the hotel booking is 50 % higher than on the Greece website. The German consumer is discriminated in terms of price. This form of cross-border price discrimination is also known as "Third Degree Price Discrimination".

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<sup>44</sup> See: R. Sinkovics, Mo. Yamin, M. Hossinger, Cultural Adaptation in Cross Border E-commerce: A study of German Companies, *Journal of Electronic Commerce Research* 2007, p. 221 ff.

<sup>45</sup> For more details to implementation of differentiation online, see: Study on business practices, p. 70 ff.

<sup>46</sup> Mystery shopping evaluation (2009), p. 6.

<sup>47</sup> Study on business practices applying different condition of access based on the nationality or the place of residence of service recipients (2009), p. 18 f.

<sup>48</sup> If the Consumer wants to purchase a specific product, this follows to a discrimination by refusal to sell or supply.

### Price discrimination after re-routing

Businesses generally use four different pricing strategies<sup>49</sup>:

- computing an average price across all source markets;
- differentiating between domestic and cross-border source markets;
- differentiating between all source markets or
- refraining from entering some source markets either completely or with a like-for-like service.

If price discrimination is practiced, the difference in price between the various national e-shops is significant. The "Study on business practices applying different conditions of access based on the nationality or the place of residence of service recipients" provides a few examples for the purchase of the Apple iPod Touch, car rental and hotel booking. A difference of 49.32 EUR emerged, for example, from a price comparison of an Apple iPod bought on apple.uk and apple.de.<sup>50</sup> The same study found that a hotel reservation made using TUI in the United Kingdom and Germany respectively resulted in a difference of EUR 210.84<sup>51</sup>. Furthermore, investigations revealed differences in price of 16 % to 22 % in the car rental sector<sup>52</sup>.

Price discrimination should not, however, be confused with differences in price applied in different Member States<sup>53</sup>. Simply, because business A sells product x in Germany for a higher price than business B in Poland does not mean that business A discriminates. Price discrimination only exists where the same business applies different prices in different Member States.

### Discrimination by range or quality of product after re-routing

Another possible form of discrimination can result from offering consumers from one Member State a completely different selection of products than those offered in another Member State. As before, this is achieved through the re-directing of the consumer from a foreign e-shop to a satellite e-shop based in his or her home Member State. Due to the fact that only goods of a certain selection are on sale, this can be seen as discrimination by refusing to sell. This will, however, only affect the consumer who is searching for a specific product.

A possible variation of this business model is to offer the same product in several Member States, but in various degrees of (poorer) quality. Such a model is, however, only possible for certain product groups and, as a result, does not play an important role in online commerce. Discrimination through differences in quality is generally not possible for the majority of products available on-line (electronics, clothes, books etc.<sup>54</sup>).

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<sup>49</sup> Study on business practices (2009), p. 5 and 32 ff.

<sup>50</sup> Study on business practices (2009), p. 22.

<sup>51</sup> Study on business practices (2009), p. 26.

<sup>52</sup> Study on business practices (2009), p. 13.

<sup>53</sup> For an overview over the differences in price levels between countries, see: Functioning of the market for electric and electronic consumer goods (2012), p. 18 f., and: Comparing the prices of electric appliances across the European Community (2009).

<sup>54</sup> For a list of the most popular categories for online-shopping products, see: Consumer Markets Scoreboard: Making Markets Work for Consumers, 3rd edition (2010), p. 22.



### 1.3.3. Discrimination by diversifying contractual conditions

The second business model capable of discriminating between consumers of different Member States could occur through a single on-line shop open to international consumers. In such a case, the consumer is discriminated against internally. In 94 % of cross-border sales, the seller successfully delivers the goods to the consumer<sup>55</sup>. This represents clear progress over the past decade, since in 2003 the success rate of delivery in cross-border transactions was only 66 %<sup>56</sup>.

Nevertheless, the possibility to discriminate exists here as well. Three possibilities for discrimination will be discussed in the context of payment options, delivery options and delivery costs.

#### Payment Options

Payment by credit card (at least VISA and MasterCard) is generally accepted in 63 % of tested e-shops<sup>57</sup>. Discrimination takes place in relation to the so-called out-dated forms of payment (invoice, *Lastschrift* in Germany, Visa Electron in the United Kingdom or Poland). These payment options are in most cases only open to the national consumer to the extent that they are still offered at all. Differences in terms of payment options are apparently adapted to the preferences of national consumers and are therefore quite diverse<sup>58</sup>.

Furthermore, there is always the possibility that hidden discrimination lurks behind payment options.

For example, the business could add an additional charge for the chosen payment option of a foreign consumer which the national consumer does not have to pay. The total price for the foreign consumer would be artificially increased and the business would actually "pocket" the additional charge with which it is, in fact, not burdened. An illustrative and fictive example for this would be the case of a consumer resident in Greece, who tries to order a product from an Italian online-shop. Although able to complete the ordering-process, the consumer is redirected to the payment-site where the final price includes an additional "foreign payment fee" of 5 %.

#### Delivery options

Various delivery options offer the opportunity to discriminate between national and international consumers. It is therefore conceivable that the national consumer would be offered more delivery options, such as express delivery or different couriers, whereas the international consumer would be limited to the standard delivery option<sup>59</sup>.

However, since as a rule, businesses make the consumer bear the costs of delivery, the significance of this form of discrimination is greatly reduced.

#### Delivery costs

Higher delivery costs for foreign consumers are the classic form of discrimination. However, these costs are generally in the nature of cross-border transactions, since the cost of delivering to national consumers is significantly cheaper than delivery to consumers in other Member States. As a consequence, differences in price are, generally speaking, justified. However, this reason is difficult to understand in border areas, because the price

<sup>55</sup> Online Cross-Border Mystery Shopping - State of the e-Union (2011), p. 29.

<sup>56</sup> Realities of the European online marketplace - A cross-border e-commerce project by the European Consumer Centre's Network (2003), p. 11.

<sup>57</sup> Mystery shopping evaluation (2009), p. 45 ff.; for a statistical analysis on the payment options offered, see: Online Cross-Border Mystery Shopping (2011), p. 16 f.

<sup>58</sup> Mystery shopping evaluation (2009), p. 45 ff.

<sup>59</sup> Mystery shopping evaluation (2009), p. 49 ff.

between national delivery and cross-border delivery is significantly different and does not take distance into account. For example, a 2 kg parcel from Aachen (Germany) to Berlin (Germany) costs EUR 6.90<sup>60</sup> and has a route by around 600 km. A 2 kg parcel from Aachen (Germany) to Maastricht (Netherlands) costs EUR 17.00<sup>61</sup> and has a route of around 40 km. However, the origin of this problem is not to be found in the business strategy of retailers; but rather in the parcel delivery market and their pricing strategies<sup>62</sup> and delivery practices<sup>63</sup>.

The average rate of shipping costs cross-border is EUR 16 and EUR 8 domestically<sup>64</sup>. While 29 % of domestic shops offer free delivery, the figure for cross-border shops was just 5 %<sup>65</sup>.

Such discrimination occurs, for example, when a consumer resident in Malta wants to order from an English online-shop. She is allowed to buy, but at the last step, she has to pay EUR 60 for delivery to Malta. The real shipping costs are perhaps one third of that sum. The consumer is discriminated against and has no real possibility of buying from the English online-shop.

Similarly, if a consumer from Luxemburg wishes to buy an article for EUR 19.34 with delivery costs amounting to EUR 5.00 from a business using the internet platform provided by yatego.com. This is, however, only possible if the consumer selects the option "Luxemburg surcharge" (as termed by the e-shop) which amounts to an extra EUR 26.00<sup>66</sup>.

With respect to delivery costs, discrimination is not necessarily practiced by the seller. The prices charged by haulage companies play an important role<sup>67</sup>. There is a two-tier market for EU cross-border parcels<sup>68</sup>. Large retailers with large and predictable traffic profiles often enjoy the benefits of competitive markets and economies of scale (the larger the volume, the lower the price)<sup>69</sup>. Businesses which send low parcel volumes infrequently, or operate from peripheral countries and non-urban areas, have to pay higher prices than large retailers<sup>70</sup>.

There are significant differences in the catalogue prices of haulier businesses. For example, the domestic price of sending a 2kg parcel within the sender country is very different (Cyprus EUR 1.28; Hungary EUR 3.81; Poland EUR 4.27; Germany EUR 6.90; UK EUR 12.63)<sup>71</sup>. The average cross-border price of sending a 2kg parcel is also very different (Cyprus EUR 23.92; Hungary EUR 28.07; Poland EUR 11.22; Germany EUR 17.00; UK EUR 18.51)<sup>72</sup>. This shows that alone due to the varying shipping prices practiced within the EU the selling business does not necessarily profit from practicing higher delivery costs for consumers residing in other Member States.

Nevertheless, a hidden form of discrimination may lie behind the delivery costs applied by a business. It is thus conceivable that delivery costs are set at (significantly) higher levels

<sup>60</sup> Intra-Community cross-border parcel delivery (2011), p. 164 ff. and 277.

<sup>61</sup> Intra-Community cross-border parcel delivery (2011), p. 164 ff. and 277.

<sup>62</sup> See: Intra-Community cross-border parcel delivery (2011), p. 158 ff.; Main developments in the postal sector (2008-2010), p. 36 ff.

<sup>63</sup> See: Main developments in the postal sector (2008-2010), p. 203 ff.

<sup>64</sup> Mystery shopping evaluation (2009), p. 5.

<sup>65</sup> Mystery shopping evaluation (2009), p. 54.

<sup>66</sup> A reported illustrative case from the ECC Network.

<sup>67</sup> For a further analysis, see Pricing behaviour of postal operators (2012).

<sup>68</sup> Intra-Community cross-border parcel delivery (2011), p. 6.

<sup>69</sup> Intra-Community cross-border parcel delivery (2011), p. 6 and 116 ff.

<sup>70</sup> Intra-Community cross-border parcel delivery (2011), p. 6 and 116 ff.

<sup>71</sup> Intra-Community cross-border parcel delivery (2011), p. 164 ff. and 277.

<sup>72</sup> Intra-Community cross-border parcel delivery (2011), p. 164 ff. and 277.



than is actually the case. Such a business would be enriched at the expense of consumers from different Member States. This type of discrimination cannot be justified. It may, however, be accounted for as a concealed means of accounting for the additional costs which loom over cross-border transactions. The extent to which this form of discrimination actually takes place cannot be evidenced in a study of this nature. Offering goods only with significantly higher delivery costs businesses may, in effect, be seen as a refusal to sell.

#### 1.4. Intermediaries and consumer confidence to DSM

In December 2012, there were 57,389 million German internet users, over 53,6 million of whom used Google<sup>73</sup>. Over the past 12 months<sup>74</sup>, 81 % of online consumers used a price comparison website in die EU<sup>75</sup>. Primarily, consumers used the price comparison websites (PCW) to compare prices (74 %), make savings (59 %) and find the best deals (55 %)<sup>76</sup>. These statistics reveal the central role played by search engines and price comparison websites for internet users and also for the DSM.

##### 1.4.1. Impact of search engines

Intermediaries such as e.g. Google offer separate search engines for each Member State. When a consumer enters google.com as a web address, his or her current location is pinpointed through the IP-address of the computer used and the consumer is re-directed to the corresponding search engine of that particular Member State. The effect of this automatic re-direction is, however, limited by the fact that most users normally use the address of the search engine of their Member State (i.e. in Germany, google.de). Additionally, the conscious decision of a consumer located in Germany to use [google.co.uk](http://google.co.uk) does not lead to automatic re-direction to [google.de](http://google.de).

The results of a Google search are presented by means of a specially adapted algorithm which is not in the public domain<sup>77</sup>. Known parameters such as the geographical location of the server and the language of the search are particularly relevant. Consequently, results originating in the Member State of the consumer are manifestly prioritised. For example, a search for „iPhone 5“ on [google.de](http://google.de) prioritises the sites of national providers. This is also the case for the search engine versions of other Member States.

The fundamental issue for the DSM is brought into focus when a consumer wishes to buy a particular type of product and resorts to an internet search engine for preliminary information<sup>78</sup>. Since a search machine does not limit its results to purely informative sites, but also shows online-shops and advertising geared to the consumer's search, search machines such as Google can have a strong influence on the purchasing decisions of consumers. Given the fact that the websites, online-shops and advertising operating around the consumer's location are prioritised, the consumer is not given the means of discovering international on-line shops. The influence of search machines on consumers is thus limited to national offers.

In this way, Google discriminates between both consumers as well as e-shop businesses of other Member States who are excluded from the results of searches made by foreign

<sup>73</sup> 2013 Future in Focus - Digitales Deutschland, p. 18 and 28.

<sup>74</sup> Data collected between December 2010 and February 2011.

<sup>75</sup> Consumer market study (2011), p. 61.

<sup>76</sup> Advertising of Prices (2010), p. 93.

<sup>77</sup> For an attempt to find all the parameters of the Google algorithm, see: <http://www.searchenginejournal.com/200-parameters-in-google-algorithm/15457/>.

<sup>78</sup> 30% of consumers used a search engine to research their online purchase, see Consumer market study (2011), p. 49 f.

consumers. In effect, this can affect the proper functioning of the Internal Market and the potential benefits of the DSM remain unexploited.

#### 1.4.2. Impact of Price Comparison Websites (PCW)

Similar findings exist for PCW which limit the offers returned following a search to national shops. Only 11 of 233 anonymous shoppers who visited a PCW rated it as “most useful” in terms of listing cross-border offers<sup>79</sup>. The evaluation of PCW in 22 EU countries showed that only 41 % of PCW were rated as providing consumers with reliable and trustworthy information<sup>80</sup>. As a matter of fact, the national consumers might not be certain about PCW results and are not able to gain adequate information as to the products and their possibly cheaper alternatives from other Member States.

Price comparison websites are of much greater importance to the DSM. Whereas Google is primarily used for conducting preliminary research into products, PCW are used directly before the decisive moment, the point at which the consumer actually buys a product online. According to current statistics, quite a number of consumers use PCW in deciding where to buy their products from. The average consumer is not at all aware of any discrimination taking place as a consequence of PCW limiting their search results to those offers available nationally. In general, consumers are thus not aware of the possibility of significantly cheaper offers outside of their own Member State.

As is the case with search engines, the way in which price comparison websites work does not only affect consumers; businesses who wish to offer their products abroad are also affected. Such foreign businesses will not even appear on the radar of a consumer who is trying to shop around. Since the offers appearing after an enquiry using a PCW are limited to national offers, this effectively prevents the emergence of advertising on a European level, discriminating both against consumers and businesses. National businesses are thus given an unfair advantage as, at least in the context of PCW, they only need compete with other national businesses and so do not need to engage in competitive pricing in relation to the offers of foreign business. This could therefore lead to higher prices for the consumer.

In the world of the PCW, the single market does not exist. However, given the relatively important role played by PCW in the decision-making process of consumers, there is great potential for development in this field. In the long-term, internationally oriented PCW could greatly contribute to the creation of a true DSM.

A central reason for PCW not including the offers of businesses based in other Member States is the trust of consumers<sup>81</sup>. If the sale concluded by the consumer with a foreign business leads to problems, this will backfire on the PCW which included that business's offer. The PCW thus has a direct commercial interest in excluding internationally available offers. Given that cross-border offers are often cheaper, the inclusion of these offers alongside national offers could weaken the national market and even oust national businesses from the market (which are nonetheless the biggest clients of PCW)<sup>82</sup>. Even if higher prices are practised abroad, the PCW still loses out, since the foreign businesses have no incentive to pay the PCW to include their offers<sup>83</sup>.

There are also practical reasons which militate against comparing international offers. For example, connection standards, safety standards, power cords etc. vary between Member States. Furthermore, some markets are more developed than others. This makes it

<sup>79</sup> Consumer market study (2011), p. 82.

<sup>80</sup> Consumer Market, December 2012, SWD (2012) 432, p. 55.

<sup>81</sup> Consumer market study (2011), p. 83.

<sup>82</sup> Consumer market study (2011), p. 84.

<sup>83</sup> Consumer market study (2011), p. 84.

more or less difficult for PCW to collect information on products and prices which are available in other Member States<sup>84</sup>.

### **1.5. Summary**

A comprehensive analysis of market studies shows that there is a great deal of consumer discrimination practiced in the DSM. Three practices which discriminate against groups of consumers are common: refusal to sell, automatic re-routing, and the unjustified application of different terms and conditions. Technological development also creates or encourages the emergence of new forms of discrimination (collection and analysing of data, especially data collection in conjunction with social media). The reasons for the differences in pricing and access are, according to statements from businesses, multifarious. Search engines and PCW play also an important role for the creation of a non-discriminatory DSM.

The problem of consumer discrimination in the DSM is especially important, because for 56 % of consumers a reason for buying cross-border is that the particular product in question could not be sourced in the national market. To use the potential of the DSM and to reduce the frustration of consumers, it is necessary to take measures to reduce the discrimination of consumers in an effective way.

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<sup>84</sup> Consumer market study (2011), p. 83.

## 2. FUNDAMENTAL RIGHTS AND FREEDOMS - ARTICLE 20 (2) OF SERVICES DIRECTIVE

### KEY FINDINGS

- The anti-racism provisions of the Treaty and of secondary law are usually not infringed by a service provider's refusal to accept orders of consumers from other Member States. The consumers' interest at stake is usually not their dignity; it is simply their right to participate in the internal market. Only in exceptional cases, where refusal to sell infringes the dignity of consumers is it possible for the provisions against discrimination on grounds of race and ethnical origin of the Treaty and of secondary law to have been infringed. This is the usually the case where a service provider generally refuses to accept orders from nationals of a certain state (irrespective where they are resident). Such arbitrary discrimination displays contempt for the citizens of a certain state on the mere ground that they are citizens of that state and is therefore prohibited.
- Article 18 of the TFEU explicitly contains a directly applicable, autonomous, absolute and general prohibition of discrimination on grounds of nationality and in paragraph (2) a power allowing for the introduction of further specific prohibitions of discrimination. In cases where the legislation of the Member States made rights or benefits dependent on the residence of persons in a certain Member State, the ECJ has considered this as indirect discrimination on grounds of nationality since such rules are liable to operate mainly to the detriment of nationals of other Member States.
- Article 18 TFEU is undoubtedly directly applicable against the Member States and the EU itself. The ECJ has carefully extended the direct applicability of several of the fundamental freedoms to private entities, in particular powerful associations, including trade unions. In a few cases, the free movement of persons has also been directly applied to individual employers. It remains to be seen whether this line of jurisprudence will also be extended to individual service providers in the DSM. Such an extension would have to be balanced against the fundamental rights of the businesses concerned and would therefore only be feasible in cases where improvements in the functioning of the internal market outweigh the fundamental rights of the affected businesses.
- The fundamental freedoms of the Treaty usually do not defend customers against discriminatory practices of service providers in the DSM. They give market participants the freedom to make use of the internal market. Their purpose is usually not to force market participants to use this freedom fully. The fundamental freedoms usually do not protect one market participant (here: the customer) from another (here: the business which refuses to sell or only sells on less favourable terms). The few exceptions presently formulated by the ECJ concern powerful associations or trade unions, perhaps also individual employers, but not service providers in the DSM. Except for the case of infringements of anti-racism law or of a dominant position which would trigger competition law provisions, service providers in the DSM are not bound by the fundamental freedoms to provide services to market participants in other Member States. However, the fundamental freedoms constitute an important element when balancing different objectives of EU law, such as e.g. the freedom of businesses to choose whom to do business with or the protection of intellectual property.

- Article 20 (2) of Services Directive prohibits general conditions of access to a service, containing discriminatory provisions relating to the nationality or place of residence of the recipient. However, this provision is severely misconceived. Nearly every aspect of the provision is entirely unclear. It is already questionable whether it is applicable merely to services in a narrow sense or also to the sale of goods. It is, moreover, entirely unclear what constitutes a direct justification by objective criteria, which allows for differences in the conditions of access.
- Aside from infringements of the anti-racism legislation and of competition law, any economic reason for the refusal to accept orders from another Member State which has been formed autonomously by the decision-makers of a service provider may form a direct justification by objective criteria in the sense of Article 20 (2) of Services Directive. This is even true for purely digital services which do not require any physical transportation.
- It needs to be considered whether the part on discrimination based on residency in Article 20 of the Services Directive (or the whole Article) should be repealed – and not replaced by another potentially oppressive (and rather imprecise) rule, but by further unification of the national laws, diminishing some of the actual obstacles to cross-border commerce in the DSM.
- The Common European Sales Law and recent ADR/ODR legislation are steps in the right direction of removing the obstacles of the DSM instead of putting pressure on businesses to extend their activities to the whole territory of the EU. In particular the Common European Sales Law which will be an optional instrument and therefore leaves it to the parties to a contract to decide whether to make use of it or not, does not operate by forcing all businesses that make use of it to extend the scope of their activity to the whole territory of the EU. When using the Common European Sales Law, businesses remain principally free to limit their activities to a range of certain countries.

## 2.1. Fundamental rights and freedoms - overview

Discrimination of consumers in the DSM may be assessed under three distinct, but interwoven basic principles of the Treaty and the Charter, namely

- the protection of human rights (i.e. rights of every human being, specifically: the right not to be discriminated against on grounds of race or ethnic origin)<sup>85</sup>;
- the protection of citizens' rights (i.e. rights of every citizen of the EU, specifically: the right not to be discriminated against on grounds of nationality of a certain Member State)<sup>86</sup>; and
- the fundamental freedoms of the internal market which are – in principle – also granted only to EU citizens and not to all humans (specifically: the free movement of persons and services)<sup>87</sup>.

In addition to these fundamental provisions of the Treaty and the Charter, Article 20 of the Services Directive contains provisions against the discrimination of recipients of services on grounds of their nationality or place of residence. This directive is based on provisions in the EC Treaty (the predecessor of the TFEU) relating to the freedom of establishment and

<sup>85</sup> Cf. Art. 19 TFEU, Art. 21 (1) of the Charter.

<sup>86</sup> Cf. Art. 18 TFEU, Art. 21 (2) of the Charter.

<sup>87</sup> Cf. Art. 45 of the Charter.

the free provision of services<sup>88</sup>. It thus belongs to EU measures for the implementation of the fundamental freedoms and has to be interpreted in this light.

Insofar as private actors in the internal market rather than Member States are concerned, any right of consumers or other customers not to be discriminated against by traders in the DSM must be balanced against the fundamental rights of private persons (irrespective of whether legal or natural) when conducting a business, namely

- private autonomy and freedom of contract;
- the right to provide services (which might include the 'negative' right not to provide services in certain regions)<sup>89</sup>;
- the freedom to conduct a business<sup>90</sup>.

The purpose of this chapter is to examine the extent to which these fundamental provisions of the Treaty and Article 20 of the Services Directive provide effective tools in combating consumer discrimination in the DSM. The line of thought follows what can be seen as a hierarchy of the concerned rights and freedoms, starting with human and fundamental rights aspects, follows by citizens' rights and lastly the freedoms aiming at the creation of the internal market.

## 2.2. Usually no infringement of consumers' human rights

Refusal to sell in a certain Member State may – in theory – infringe the prohibition of discrimination on grounds of race or ethnic origin which is firmly anchored in Article 19 TFEU, Article 21 (1) of the Charter and in the Antiracism Directive 2000/43/EC. However, the mere commercial decision of a business not to be active on one side of any given border between Member States does not usually infringe the dignity of the people living on the other side of the border. The consumers' interest at stake is usually not their dignity; it is simply their right to participate in the internal market. Only in exceptional cases, where refusal to sell infringes the dignity of consumers is it possible for the provisions against discrimination on grounds of race and ethnical origin of the Treaty and of secondary law to have been infringed. An example could be communication of an aggressive and offensive nature (e.g. "We do not sell to Ruritania, because of our prejudice towards them"). Another example would be discrimination on grounds of nationality irrespective of where the person lives (e.g. "We do not sell to the citizens of Ruritania, irrespective of where they live"), because this would indirectly display contempt for the citizens of a certain state on the mere ground that they are citizens of that state. It is precisely such inhuman practices against which the prohibition of discrimination on grounds of race or ethnic origin is directed. The existence of such cases has not been made aware to the authors of the study. It should also be noted that any discrimination as illustrated in the examples would be prohibited irrespective of whether Ruritania is a Member State of the EU or not. Since the fundamental freedoms, the basic pillars of the internal market, – in principle – only address citizens of the EU Member States who are at the same time EU residents it should be evident that the prohibition of discrimination on grounds of race or ethnic origin does not aim at and actually does not help in improving the internal market.

<sup>88</sup> Art. 47 (2) and Art. 55 of the EC Treaty.

<sup>89</sup> Art. 15 (2) of the Charter.

<sup>90</sup> Art. 16 of the Charter.



### 2.3. Fundamental rights of businesses

Any EU action which aims at improving the internal market by putting pressure on businesses in order to push them across borders within the EU needs to be balanced against the fundamental rights of businesses. The freedom to conduct a business and the freedom to provide services in every Member State are part of the fundamental rights recognized by the law of the EU<sup>91</sup>. Article 15 (2) of the Charter of Fundamental Rights of the European Union<sup>92</sup> refers to the freedom to provide services. The freedom to conduct businesses is governed by Article 16 of the Charter<sup>93</sup>. These specific freedoms result from the right to liberty<sup>94</sup>, which is not explicitly expressed in the Charter<sup>95</sup>, but which the ECJ assumes as intrinsically linked to the Charter of Fundamental Rights<sup>96</sup>. It is a longstanding rule of ECJ case law, reiterated on many occasions, that the freedom to pursue a trade or profession forms part of the general principles of EU law and includes, as a specific expression of that freedom, the freedom to choose whom to do business with<sup>97</sup>.

Also at the level of national laws, the freedom to conduct a business is well protected. An important aspect of this protection is in particular the freedom of contract, which is one of the deepest rooted principles of the national private laws, usually protected both by the national constitutions and the – often older – civil codes<sup>98</sup>. The freedom of contract is also one of the aspects of the general principle of liberty<sup>99</sup>. This means that the decision to make a contract, with whom a person contracts and also on what terms a person contracts

<sup>91</sup> ECJ Case 151/78 (Nykøbing) from 16.01.1979, ECR 1979 - 00001, Para. 20; Case 240/97 (Spain/Commission) from 6.10.1999, ECR 1999 I-6571, Para. 99; C. Nowak, in: S. M. Heselerhaus, C. Nowak, § 31, Para. 5, 33; H. D. Jarass, Charta der Grundrechte der Europäischen Union, Commentary, Munich 2010, Art. 16, Para. 2; T. Sasse, Die Grundrechtsberechtigung Juristischer Personen durch die unternehmerische Freiheit gemäß Art. 16 der Europäischen Grundrechtecharta, EuR 2012, p. 628.

<sup>92</sup> Charter of Fundamental Rights of the European Union (2000/C 364/01), Official Journal of the European Communities from 18.12.2000.

<sup>93</sup> N. Bernsdorff, in: J. Meyer, Charta der Grundrechte, vol. II, Baden-Baden 2006, Articles 15-16.

<sup>94</sup> W. Kiemel, in: H. von der Groeben, J. Schwarze, Kommentar zum EUV/EGV (Commentary on the TEU/ECT), 6. ed., Baden-Baden 2006, Chapter 4, Para. 1-4; C. Nowak, in: S. M. Heselerhaus, C. Nowak, Handbuch der Europäischen Grundrechte, Munich 2006, § 31, Para. 5, 33.

<sup>95</sup> H. D. Jarass, Introduction, Para. 35 and Art. 7, Para. 3; J. Meyer, Charta der Grundrechte der Europäischen Union, vol. II, Art. 1, Para. 34.

<sup>96</sup> Joined Cases 133-136/85 (Rau) ECR 1987 - 2289, 2338, p. 2148, reasons 15 and 19 for the decision; ECJ Case 151/78 (Nykøbing) ECR 1979 - 00001, Para. 19; Case 240/97 (Spain/Commission), ECR 1999 I-6571 Para. 99; H. D. Jarass, Art. 16, Para. 1; M. Ruffert, in: C. Calliess, M. Ruffert, Commentary on EUV/AEUV (TEU/TFEU), Munich 2011, Art. 16 Charter of Fundamental Rights, Commentary, Para. 2.

<sup>97</sup> Cf. Case 44/79 (Hauer) ECR 1979, p. 3727, Paras 31 to 33; Case 265/87 (Schraeder) ECR 1989, p. 2237, Para. 15; Joined cases C-90/90 and C-91/90 (Neu) ECR 1991 Page I-3617, Para. 13.

<sup>98</sup> C. von Bar, E. Clive, Principles, Definitions and Model Rules of European Private Law, Draft Common Frame of Reference Full Edition, II.-1:102, p. 131 Note 1: « The freedom of the parties to make the contract and provide the contract terms they wish is recognised in all the Member States. It is provided in art. 2(1) of the GERMAN Constitution. In addition, it is found in art. 5(1) of the GREEK Constitution and in art. 361 of the Greek CC. However, according to art. 3 of the Greek CC "mandatory rules cannot be set aside by the volition of the parties." It is also provided for in the old DANISH code "Danske Lov" of 1683 in § 5.1.1; in FRENCH, BELGIAN and LUXEMBOURG law (where the freedom of the parties can be derived from CC 's art. 1134(I) on the binding effect of valid contracts); in the ITALIAN CC art. 1322; the NETHERLANDS CC art. 6:248; the PORTUGUESE CC art. 405; the SLOVENIAN LOA §§ 2 and 3; the POLISH CC art. 353<sup>1</sup>; the SLOVAKIAN CC § 2(3) and Ccom § 263; and the SPANISH CC art. 1255. It is elevated to a governing principle in the "Projet de Reforme du Droit des Contrats" published by the FRENCH Ministry of Justice in July 2008 (arts. 15 and 16). Under AUSTRIAN law, freedom of contract exists as a constitutional principle and is underpinned by § 859 of the CC. Freedom of contract is expressly stated in the BULGARIAN LOA (art. 9). In Member States where no statutory provision can be invoked, freedom of contract is a basic principle: e.g. for ENGLAND, see Chitty on Contracts I, nos. 1-011-1-012. However, freedom of contract exists only within the limits set by the mandatory rules. In modern law considerations of policy, notably the need to protect the weaker party to a contract, have led to many statutory restrictions of contractual freedom. See: the materials collected from English, French, German and other legal systems by H. Beale etc. Contract Law, Oxford and Portland 2010, pp. 39-44; See an example of Germany: H.-W. Eckert, H. G. Bamberger, H. Roth, Commentary on the BGB, 2005, § 145, Para. 8-11.

<sup>99</sup> H. D. Jarass, Art. 16, Para. 1.

is well protected by the fundamental rights resulting both from the law of the EU and from the member states.

Of course, national laws as well as the law of the EU do not grant freedom of contract without limitation. Examples are anti-discrimination law, mandatory provisions<sup>100</sup> or the provisions on invalid standard terms<sup>101</sup>. It has to be noted, however, that the vast majority of such restrictions only apply to the content of contracts. The freedom to decide on whether to conclude a contract or not is only restricted in very rare and severe cases. The main examples are discrimination on certain grounds (such a race ethnic origin, gender etc.) or the obligation to contract in cases where fundamental needs (such as water supply) would otherwise be endangered<sup>102</sup>.

## 2.4. Right of EU citizens not be discriminated under Article 18 TFEU

### 2.4.1. Legislative competence in Article 18 (2) TFEU not made use of

Whereas Article 18 (1) TFEU prohibits any discrimination based on grounds of nationality, Article 18 (2) TFEU grants the EU competence for legislation to prohibit such discrimination. Irrespective of the extent to which this competence would allow for the enactment of legislation for improving the DSM, it has to be noted that, until present, the EU has hardly made use of this legal basis. In particular the Services Directive, which is the most far reaching secondary act against consumer discrimination in the internal market, is not based on Article 18 (2) TFEU (or its predecessor which was Article 12 EC Treaty).

It might perhaps be added that the EU legislator was correct in its parsimony; Article 18 (2) seems to be a general default competence which is subsidiary in relation to the more specific competences related to the fundamental freedoms. In particular the Services Directive has been based on Article 47(2) and Article 55 of the EC Treaty. These are provisions relating to the freedom of establishment and the free provision of services, which – at least in the view of some authors in legal writings – block Article 18 (2) TFEU due to the *lex specialis* rule<sup>103</sup>.

### 2.4.2. “Within the scope of application of the Treaties”

The prohibition of discrimination on grounds of nationality, which is now regulated in Article 18 TFEU, has been called by the ECJ a basic principle of Union law<sup>104</sup>. Legal writers often refer to it as a *leitmotiv* of the Treaty<sup>105</sup>. The prohibition of discrimination on grounds of nationality (Article 18 of the TFEU only concerns EU-nationality)<sup>106</sup> is not mainly based on ethical considerations (otherwise the special protection of EU-citizens over non-EU nationals would not be justified). It is rather a basic equality provision (all citizens are equal) for all citizens of the European Union – to be regarded mainly by the Member States and the Union itself.

<sup>100</sup> Also see: Article 1 Common European Sales Law, Regulation of the European Parliament and of the Council from 11.10.2011, Com (2011) 635 final; Article 1.1. of the Unidroit Principles of International Commercial Contracts 2010; C. von Bar, E. Clive, Principles, Definitions and Model Rules of European Private Law, Draft Common Frame of Reference Full Edition, Munich 2009, II.-7:301, pp. 535-538, II.-7:302, pp. 538-547.

<sup>101</sup> Council Directive 93/13/EEC of 05.04.1993 on unfair terms in consumer contracts, Official Journal L 095, 21/04/1993, pp. 29-34.

<sup>102</sup> R. M. Beckmann, in: Staudinger, BGB, Berlin 2004, Introduction §§ 433 et seq, Para. 107; H.-W. Eckert, H. G. Bamberger, H. Roth, § 145, Para. 12-19.

<sup>103</sup> On this discussion see A. Epinay, in: C. Calliess, M. Ruffert, EUV/AEUV, 4<sup>th</sup> edition 2011, Art. 18 TFEU, Nr. 48.

<sup>104</sup> ECJ Case C-115/08 (Land Oberösterreich/ČEZ) ECR 2009 I-10265.

<sup>105</sup> Von Bogdandy, in Grabitz/Hilf (Hrsg.), EU, Art. 12 Nr. 1.

<sup>106</sup> On the relation of Art. 18 TFEU and Articles 56-62 TFEU see: V.H.S.E. Robertson, Perspektiven für den grenzüberschreitenden Dienstleistungshandel, Baden-Baden 2012, p. 104.



Article 18 (1) of the TFEU starts with the restricting phrase that it only applies “within the scope of application of the Treaties”. The reason for this limitation is that the EU itself has only limited competences in relation to the Member States which need to be taken into account when applying this article. The ECJ has produced an abundant case law on this point. For the purposes of this study it may suffice to highlight that the ECJ in particular considered issues relating to the fundamental freedoms of the internal market as being within the scope of Article 18 (or its predecessors)<sup>107</sup>. Combating consumer discrimination in the DSM is part of the internal market competence and therefore within scope of the treaties from the outset.

There are, however, two aspects which make it highly questionable whether Article 18 can operate as a legal basis for measures against consumer discrimination by businesses in the DSM. The first is that Article 18 only incriminates criteria based on “nationality” and not those based on “residence”. The second issue is the open question of whether Article 18 (1) directly applies to private persons.

#### 2.4.3. “Residence” as indirect discrimination on grounds of nationality

Article 18 (1) only prohibits discrimination on grounds of nationality; whereas – as already explained above – the main (if not only) problem is discrimination on grounds of residence. Nowhere in primary law is “residence” independently mentioned as a prohibited criterion of discrimination.

“Residence” can only be covered by Article 18 if discrimination on grounds of residence amounts to (indirect) discrimination on grounds of nationality. *Prima facie* one might tend to answer this question in the affirmative. In its landmark decision treating a distinction drawn on the basis of residence whereby non-residents were denied certain benefits which were, conversely, granted to persons residing within national territory in the case of *Schumacker*<sup>108</sup>, the ECJ held that the national rules were liable to operate mainly to the detriment of nationals of other Member States. Since non-residents are in the majority of cases foreigners, the ECJ considered, here in a tax law case, that benefits, granted only to residents of a Member State may constitute indirect discrimination by reason of nationality. Applying the criterion of residence amounts to indirect discrimination on grounds of nationality because of the simple reason that it has nearly the same effect as a rule which directly refers to nationality would have. The ECJ has repeated this doctrine several times. Important examples were:

- National legislation in a Member State laying down a reference period for entitlement to invalidity benefits which did not provide for the possibility of prolongation where the events or circumstances corresponding to those which make prolongation possible arise in another Member State (decision based on the free movement of workers, Articles 48(2) and 51 of the EEC Treaty)<sup>109</sup>.
- A provision in a Member State’s tax law which taxed a worker who resides in another Member State more heavily than a worker who resides in the first State when the worker does not receive in the second State sufficient income in a manner enabling his personal and family circumstances to be taken into account (decision based on the free movement of persons, Article 48 of the EEC Treaty)<sup>110</sup>.

<sup>107</sup> ECJ Case 293/83 (Gravier) ECR 1985 00593, Nr. 21 ss.; ECJ Case 186/87, (Cowan) ECR 1989 00195, Nr. 17; ECJ Case C-43/95 (Data Delecta) ECR 1996 I-04661, Nr. 13 ss.; ECJ Case C-147/03 (Commission/Austria) ECR 2005 I-05969, Nr. 31 ss.; ECJ Case C-73/08 (Bressol) ECR 2010 I-02735.

<sup>108</sup> Case C-279/93 (Schumacker), ECR 1995 I-00225, point 28; earlier along the same line already Elissavet Paraschi, Case C-349/87 ECR 1991 I-04501.

<sup>109</sup> Case C-349/87 (Elissavet Paraschi) ECR 1991 I-04501.

<sup>110</sup> Case C-279/93 (Schumacker) ECR 1995 I-00225.

- National legislation in a Member State concerning the assessment of tax due on the inheritance of immovable property situated in that Member State according to which, in order to assess the property's value, the fact that the person holding legal title was under an unconditional obligation to transfer it to another person who has financial ownership of that property may be taken into account if, at the time of his death, the former resided in that Member State, but may not be taken into account if he resided in another Member State (decision based on the freedom of capital, Articles 48 and 52 of the EC Treaty)<sup>111</sup>.
- A requirement in the law of a Member State that nationals of the other Member States must reside in the State concerned in order to be appointed managers of undertakings (based on the free movement of persons, Article 48 EC Treaty)<sup>112</sup>.
- A provision in a Member State prohibiting the manager of a harbour, on pain of prosecution, from renting moorings in excess of a specified quota to boat-owners who are resident in other Member States (based on the freedom to provide services, Article 59 EC Treaty)<sup>113</sup>.

Since these decisions are mainly based on individual fundamental freedoms (e.g. movement of persons, services, capital) and not on the general provision in the Treaty (which is now Article 18 TFEU, former Article 12 EC, former Article 6 EC Treaty) it may be worth looking at cases which are directly based on Article 18 TFEU and its predecessors. Important examples from the last decade were:

- Case C-75/11 (Commission v Austria), based on Article 18 TFEU, Member State in which reduced fares on public transport are granted only to students whose parents are in receipt of family allowances in that Member State.
- Case C-291/09 (Francesco Guarnieri), based on Article 18 TFEU, provision of security pending judgment, by a claimant of Monégasque nationality.
- Case C-382/08 (Michael Neukirchinger): based on Article 12 EC, condition of residence for company seat.
- Case C-123/08 (Dominic Wolzenburg): based on Article 12 EC, European arrest warrant.
- Case C-103/08 (Arthur Gottwald): based on Article 12 EC, freedom of movement of persons (annual toll discount in respect of a motor vehicle free of charge to disabled persons only if disabled persons resident or ordinarily resident in national territory).
- Case C-222/07 (UTECA): based on Article 12 EC, obligation for television operators to earmark a percentage of their operating revenue for the pre-funding of European films in one of the official languages of the Kingdom of Spain).
- Case C-158/07 (Jacqueline Förster): based on Article 12 EC, freedom of movement of persons (student who is a national of one Member State and goes to another Member State asking for student maintenance grant).
- Case C-164/07 (James Wood): based on Article 12 EC, compensation awarded by the Fonds de garantie des victimes des actes de terrorisme et d'autres infractions.

<sup>111</sup> Case C-364/01 (Heirs of H. Barbier) ECR 2003 I-15013.

<sup>112</sup> Case C-350/96 (Clean Car Autoservice) ECR 1998 I-02521.

<sup>113</sup> Case C-224/97 (Erich Ciola) ECR 1999 I-02517.

- Case C-302/02 (Nils Laurin Effing): based on Article 12 EC, child of a prisoner, conditions of granting the maintenance payment after prisoner had been transferred to another Member State to serve his sentence.
- Case C-224/00 (Commission v Italy): based on Article 12 EC, difference in treatment of persons contravening the highway code according to the place of registration of their vehicle.

This rather long line of cases – where the ECJ confirms its doctrine that a discrimination on grounds of residence can amount to an indirect discrimination on grounds of nationality – is characterised by two elements which may be worth pointing out for the specific purposes of this study.

Firstly, most cases deal with state legislation, thus abstract and general rules in which residency is a criterion for a certain right or benefit. Because of the abstract and general character of such rules, it is indeed more than likely that certain nationals are actually been discriminated against by rules on residence. Therefore the actual nationality of concrete persons resident in a certain state is not a relevant factor for assessing the discrimination. If a certain benefit is generally not granted to the residents of Ruritania, it is very likely that many nationals of Ruritania are being subject to this refusal. Therefore the rule in question can easily be qualified as discriminatory on grounds of nationality although it “only” refers to the residence of a person. This assessment may be very different in cases where individual decisions (e.g. whether to conclude a contract or not) are subject to control by state authorities or the courts. If, for instance, an individual resident of Ruritania complains that the orders he placed are not being accepted by a certain business because he is a resident of Ruritania, one may wonder whether this person is only indirectly discriminated against on grounds of nationality if he actually is a national of Ruritania. Until present, no such cases have been brought before the ECJ. It is therefore an open question whether the *Schumacker* doctrine that discrimination on grounds of residence may be considered as indirect discrimination on grounds of nationality can be applied to a case where an individual business refuses to contract with an individual customer resident in another Member State. Presently, the doctrine that discrimination on grounds of residence can qualify as indirect discrimination on grounds of nationality only applies to abstract and general rules, not to individual decisions.

Secondly, all cases mentioned until now deal with legislation or rule-making activities of public bodies and not of private persons. There are some cases where the ECJ carefully extended the obligations arising out of the fundamental freedoms to private entities which must now be discussed. The extent to which the *Schumacker* doctrine (under which discrimination on grounds of residence may be considered as indirect discrimination on grounds of nationality) can be applied without appropriate modifications or adaptations to private persons must be evaluated. This is particularly important since private persons – unlike the state – are protected by their fundamental rights such as freedom of contract.

#### 2.4.4. Direct applicability of Article 18 (1) of the TFEU on private persons?

In relation to the Member States, Article 18 (1) of the TFEU is directly applicable in the sense that this article grants individuals rights against the Member States which can be invoked in the national courts<sup>114</sup>. However, Article 18 (1) of the TFEU is principally addressed to the Member States and the legislature of the EU<sup>115</sup>. Consequently, only action

<sup>114</sup> ECJ Case 26/62 (Van Gend & Loos); Case C-17/91 (Lornoy) ECR 1992 I-06523, point 24; case C-122/96 (Saldanha) ECR 1997 I-05325, point 15; case C-274/96 (Bickel) ECR 1998 I-07367, point 31; case C-234/99 (Niels Nygård) ECR 2002 I-3657, point 51.

<sup>115</sup> See for example (with respect to the free movement of goods), Case 311/85 (Vereniging van Vlaamse Reisbureaus) ECR 1987, p. 3801, Para 30; Case C-159/00 (Sapod Audic) ECR 2002, p. I-5031, Para. 74.

taken by the Member States or the EU can in principle be measured against the fundamental freedoms<sup>116</sup>. The ECJ has taken a rather broad view on the concept of measures taken by Member States. For instance, measures taken by professional organisations have been examined for their compatibility with the fundamental freedoms where, under national law, those organisations have been granted powers similar to sovereign powers<sup>117</sup>. Measures taken by legal persons established under private law and controlled, directly or indirectly, by the Member State concerned are also deemed to be public measures attributable to that Member State<sup>118</sup>.

In some cases the ECJ has also shown a tendency to enlarge the scope of the fundamental freedoms indirectly to include, in special circumstances, action taken by private individuals, even though they do not exercise any powers similar to sovereign powers<sup>119</sup>.

Important examples are:

- Case 36-74 (Walrave and Koch): Free provision of services; prohibition of discrimination does not only apply to the action of public authorities but similarly extends to rules of any other nature aimed at regulating in a collective manner remunerated employment and the provision of services (here: requirements of an association of cycling federations that participants in teams at world cycling championships must be of the same nationality).
- Case C-415/93 (Bosman): Freedom of movement of workers; rules of football associations, limitation of the number of players having the nationality of other Member States who may be fielded in a match.
- Case C-309/99 (Wouters): Competition and freedom to provide services; national Bar; regulation by the Bar of the exercise of the profession; prohibition of multi-disciplinary partnerships between members of the Bar and accountants.
- Case C-519/04 (Meca-Medina and Majcen v Commission); Competition and freedom to provide services; rules adopted by the International Olympic Committee concerning doping control; Incompatibility with the Community rules on competition and freedom to provide services.
- Case C-438/05 (Viking): Right of establishment; collective action taken by a trade union organisation against a private undertaking; collective agreement liable to deter an undertaking from registering a vessel under the flag of another Member State.
- Case C-341/05 (Laval): Posting of workers; collective agreement for the building sector; possibility for trade unions to attempt, by way of collective action, to force undertakings established in other Member States to negotiate in order to determine the rates of pay for workers and to sign the collective agreement for the building sector.
- Case C-325/08 (Olympique Lyonnais): Freedom of movement for workers ; professional football players ; obligation to sign the first professional contract with the club which provided the training.

<sup>116</sup> Opinion of Advocate General Trstenjak in Case C-171/11 (Fra.bo), Para. 29.

<sup>117</sup> Joined Cases 266/87 and 267/87 (Association of Pharmaceutical Importers) ECR 1989, p. 1295, Para. 13 et seq.; Case C-292/92 (Hünernund) ECR 1991, p. I-6787, Para. 12 et seq.

<sup>118</sup> Cf. e.g. Case C-325/00 (Commission v Germany) ECR 2002, p. I-9977, Para. 14 et seq. ; Case 302/88 (Hennen Olie) ECR 1990, p. I-4625, Para. 13 et seq.

<sup>119</sup> This observation has been made by Advocate General Trstenjak in her Opinion on Case C-171/11 (Fra.bo), Para. 30.

- Case C-379/09 (Casteels): Freedom of movement for workers; social security for migrant workers; protection of supplementary pension rights; worker employed successively by the same employer in several Member States.
- Case C-171/11 (Fra.bo): Free movement of goods; applicability of Article 28 EC to a private-law certification body which - by virtue of its authority to certify the products - actually holds the power to regulate the entry into a national market of products.

These examples all have in common that they deal with powerful sports associations, professional associations, trade unions or similar organisations. This case law can be summarised to the extent that Articles 34 TFEU (free movement of goods) 45 TFEU (freedom of movement for workers), 49 TFEU (freedom of establishment) and 56 TFEU (freedom to provide services) apply not only to acts of official bodies, but also to bodies of rules of other kinds intended collectively to govern the import of goods, employment, self-employment and the provision of services<sup>120</sup>. If bodies of a private law nature have, within their sector, the power to enact discriminatory rules which can have the same effect on the conditions for the exercise of the fundamental freedoms as state legislation. It goes without saying that EU law cannot tolerate discriminatory rules which actually have the same effect as state legislation would have for the mere reason that the rulemaking body is not a public law body, but a private law entity.

In the area of the freedom of movement for workers, however, the ECJ took an important step towards binding private individuals further to the fundamental freedoms, in a context other than the establishment of certain kinds of collective rules. Until now there are two cases, which attracted much attention and caused much debate in legal writings<sup>121</sup>.

These cases are:

- Case C-281/98 (Angonese): Freedom of movement of persons; Article 48 of the EC Treaty precludes an employer from requiring persons applying to take part in a recruitment competition to provide evidence of their linguistic knowledge exclusively by means of one particular diploma issued only in one particular province of a Member State.
- Case C-94/07 (Raccanelli): Freedom of movement of workers; a private-law association, such as the Max-Planck-Gesellschaft zur Förderung der Wissenschaften eV, must observe the principle of non-discrimination in relation to workers within the meaning of Article 39 EC.

It needs to be noted that both cases concern employment law, where private employers are being considered to be bound to observe the principle of non-discrimination relating to the free movement of persons. The second case is, however, rather atypical, since the employer in question, the Max-Planck-Gesellschaft zur Förderung der Wissenschaften eV, is a fully state financed association, to which under the general doctrines of EU law the fundamental freedoms are applicable in any event. In the final case (Angonese), the Court

<sup>120</sup> Similarly, the Opinion of Advocate General Trstenjak in Case C-171/11 (Fra.bo), Para. 32.

<sup>121</sup> Cf e.g. R. Streinz, S. Leible, Die unmittelbare Drittwirkung der Grundfreiheiten, Europäische Zeitschrift für Wirtschaftsrecht 2000 p.459-467; U. Forsthoff, Drittwirkung der Grundfreiheiten: Das EuGH-Urteil Angonese, Europäisches Wirtschafts- & Steuerrecht - EWS 2000 p.389-397; C. Weber, Freizügigkeit - Zugang zur Beschäftigung, Recht der Arbeit 2001 p.183-185; L. Michaelis, Unmittelbare Drittwirkung der Grundfreiheiten - Zum Fall Angonese, Neue juristische Wochenschrift 2001 p.1841-1842; A. Lengauer, Drittwirkung von Grundfreiheiten - Eine Besprechung der Rs C-281/98, Angonese, Zeitschrift für Rechtsvergleichung, internationales Privatrecht und Europarecht 2001 p.57-65 [all sceptical with regard to a general horizontal effect of all fundamental freedoms]; W. Obwexer, EuGH: Neue Pflichten für Unionsbürger, Europäisches Wirtschafts- & Steuerrecht - EWS 2000 p. I [argues in favour of the general horizontal effect of all fundamental freedoms]; R. Lane, N. Shuibhne, Common Market Law Review 2000 p.1237-1247 [no position on general horizontal effect].

expressed the extension of the applicability of the freedom of movement of workers in the following words:

*“30 It should be noted at the outset that the principle of non-discrimination set out in Article 48 is drafted in general terms and is not specifically addressed to the Member States.*

*31 Thus, the Court has held that the prohibition of discrimination based on nationality applies not only to the actions of public authorities but also to rules of any other nature aimed at regulating in a collective manner gainful employment and the provision of services (see Case 36/74 Walrave v Union Cycliste Internationale [1974] ECR 1405, paragraph 17).*

*32 The Court has held that the abolition, as between Member States, of obstacles to freedom of movement for persons would be compromised if the abolition of State barriers could be neutralised by obstacles resulting from the exercise of their legal autonomy by associations or organisations not governed by public law (see Walrave, paragraph 18, and Case C-415/93 Union Royale Belge des Sociétés de Football Association and Others v Bosman and Others [1995] ECR I-4921, paragraph 83).*

*33 Since working conditions in the different Member States are governed sometimes by provisions laid down by law or regulation and sometimes by agreements and other acts concluded or adopted by private persons, limiting application of the prohibition of discrimination based on nationality to acts of a public authority risks creating inequality in its application (see Walrave, paragraph 19, and Bosman, paragraph 84).*

*34 The Court has also ruled that the fact that certain provisions of the Treaty are formally addressed to the Member States does not prevent rights from being conferred at the same time on any individual who has an interest in compliance with the obligations thus laid down (see Case 43/75 Defrenne v Sabena [1976] ECR 455, paragraph 31). The Court accordingly held, in relation to a provision of the Treaty which was mandatory in nature, that the prohibition of discrimination applied equally to all agreements intended to regulate paid labour collectively, as well as to contracts between individuals (see Defrenne, paragraph 39).*

*35 Such considerations must, a fortiori, be applicable to Article 48 of the Treaty, which lays down a fundamental freedom and which constitutes a specific application of the general prohibition of discrimination contained in Article 6 of the EC Treaty (now, after amendment, Article 12 EC). In that respect, like Article 119 of the EC Treaty (Articles 117 to 120 of the EC Treaty have been replaced by Articles 136 EC to 143 EC), it is designed to ensure that there is no discrimination on the labour market.*

*36 Consequently, the prohibition of discrimination on grounds of nationality laid down in Article 48 of the Treaty must be regarded as applying to private persons as well.”*



This case could be interpreted in different ways. Some formulations, in particular paras 30 and 36 of the judgement, seem to indicate that the horizontal effect of the prohibition of discrimination on grounds of nationality in Article 48 EC Treaty (now: Art 45 TFEU) applies without any further requirement to all private persons. Since the Court in para 35 expressly mentioned the general prohibition of discrimination contained in Article 6 of the EC Treaty (now in Article 18 TFEU), one might even conclude that the said general prohibition of discrimination in Article 18 TFEU applies to all private persons.

The second, restricted interpretation could point that the considerations leading to the direct applicability of the internal market provisions of the Treaty stated here are

- firstly, limited to the freedom of movement of workers (now Article 45 TFEU), and
- secondly, limited to private employers.

In legal writings it is disputed whether and to what extent Article 18 (1) of the TFEU has direct effect between private persons. Some authors consider Article 18 (1) of the TFEU generally directly applicable between private persons<sup>122</sup>. Others are more sceptical and see the Angonese case law as an exception from the rule that – in principle – the fundamental freedom and the general prohibition of discrimination on grounds of nationality do not have horizontal effect outside the rather specific situations where the ECJ expressly applied individual fundamental freedoms against certain bodies of a private law nature<sup>123</sup>.

The Court has not yet had the opportunity to clarify further. There is, in particular, no case law on the provision of services in the DSM where the Court has considered the horizontal application of Article 18 (1) TFEU or any of the fundamental freedoms to a service provider. It may, however, throw some light on the possible future approach of the ECJ to consider how the Court recently referred to the Angonese and Raccanelli Cases in its judgements or the opinions of the Advocate Generals. For instance, in Case C-172/11 (Erny), which again mainly deals with the freedom of movement of workers, the Court stated in para 36:

*“The prohibition of discrimination laid down in that provision [i.e. Article 45 (2) TFEU] applies not only to the actions of public authorities, but also to all agreements intended to regulate paid labour collectively, as well as to contracts between individuals “.*

This formulation seems to include all “contracts between individuals” in the scope of application of the freedom of movement of workers. It does, however, not mention any other of the fundamental freedoms, and in particular not the general prohibition of discrimination on grounds of nationality.

Advocate General Kokott said in her Opinion on Case C-379/09 (Casteels) in para 84:

*“According to established case-law, direct recourse to freedom of movement for workers is permitted in relation to collective agreements, including in ‘horizontal’ legal relationships between private persons.”*

<sup>122</sup> Cf. A. Wrobel, in: D. Miąsik, N. Półtorak, A. Wróbel (ed.), Traktat o funkcjonowaniu Unii Europejskiej. Komentarz, t. I. Art. 1-89, Lex on-line ed. 2012, Art. 18.3; Grabitz/Hilf (Ed.), v. Bogdandy, EU, Art. 12, Nr. 28; D.-E. Kahn, in: R. Geiger, D.-E. Khan, M. Kotzur, Art. 18, para 4; S. Leible, S. Navas Navarro, J. Pisuliński, F. Zoll, in: Principles of the Existing EC Contract Law (Acquis Principles), Contract II, Para. 4, p. 159; W.-H. Roth, in: M. A. Dausen, EU-Wirtschaftsrecht (Business law of the EU), 2012, E. I. Grundlagen (basic principles), Para. 30; W.-H. Roth, Drittwirkung der Grundfreiheiten ? (third-party effect of the fundamental freedoms ?), Festschrift for U. Everling, pp. 1245-1246.

<sup>123</sup> This seems to be the prevailing opinion, cf. A. Epinay, in: C. Calliess, M. Ruffert, EUV/AEUV, 4<sup>th</sup> edition 2011, Art. 18 TFEU, Nr. 44; M. Holoubek, in J. Schwarze, EU-Kommentar, vol. III, Baden-Baden 2012, Art. 18, Para. 2; Streinz, in: Streinz, EUV/EGV, Art. 12 EC-Treaty, Nr. 39; Zuleeg, EU/EC-Treaty, Art. 12, Nr. 17; M. Rossi, EuR 2000, pp. 216-217; see also the articles cited in Fn. 121.

Advocate General Cruz Villalón said in his Opinion on Case C-475/11 (Konstantinides) in para 37:

*“As the Court has repeatedly observed, the freedoms of movement must also be respected ‘in the case of rules which are not public in nature but which are designed to regulate, collectively, self-employment and the provision of services.’”*

Whereas the first of these two quotations is clearly limited to the free movement of workers, the second more generally deals with the “freedoms [plural!] of movement”, including the provision of services.

Advocate General Trstenjak has recently delivered several opinions relevant in this context. In her Opinion on Case C-282/10 (Dominguez) she wrote in paras 124 and 126:

*“(124) A further indication of the direct applicability of general principles in relationships between private individuals can be derived from the judgment in the Angonese case, which concerned access to employment at a private bank in which the Court took the view that ‘the prohibition of discrimination on grounds of nationality laid down in [Article 45 TFEU] must be regarded as applying to private persons’.*

*(126) In summary, it must be stated that in light of this case-law the direct application of fundamental rights in the form of general principles in relationships between private individuals cannot be ruled out in principle”.*

In her Opinion on Case C-171/11 (Fra.bo), Advocate General Trstenjak wrote in para 45:

*“In these circumstances, there are no fundamental objections to the application of the argument developed in case-law on the limited horizontal effect of the freedom of movement for workers, the freedom of establishment and the freedom to provide services to a case such as the present one, in which the applicability of the principle of the free movement of goods to a private-law association with de facto rule-making competence is at issue.”*

In particular these two quotations of Advocate General Trstenjak prove that the Court is generally contemplating the horizontal effect of fundamental rights and the fundamental freedoms. In the last quotation Advocate General Trstenjak expressly lists all the fundamental freedoms of the Treaty. She speaks, however, of the “limited” horizontal effect of the fundamental freedoms. This clearly indicates that, in her opinion, the current case law of the Court does not allow for the general statement that the fundamental freedoms have direct effect. Her analysis reveals a rather careful and sometimes reluctant approach of the ECJ to extend the horizontal effect of the fundamental freedoms.

In the view of the authors of this study, it is, in the current state of EU law, hardly feasible to generalise the ideas expressed in the Angonese case law to

- all other aspects of the internal market such as a general prohibition of discrimination on grounds of nationality as regulated in Article 18 TFEU, and
- to private persons other than employers or associations with de facto rule-making competence.

Any extension of the applicability of the fundamental freedoms to private businesses must be balanced against the fundamental rights of these businesses, in particular the freedom to pursue a trade or profession, which forms part of the general principles of EU law and includes, as a specific expression of that freedom, the freedom to choose whom to do



business with<sup>124</sup>. In the light of the case law of the ECJ the direct application of Article 18 (1) between private persons can only be assumed if private actors either have power and influence comparable to states with the effect that other private actors have hardly any chance of avoiding discrimination. This may be the case, in particular, where associations of employers discriminate on grounds of nationality or residence. It may also mean that 'simple' private employers (which do not have such power) may not impose discriminatory requirements as the defendant in the Angonese case did when organising the recruitment competition.

Only a new line of case law would allow for extension of the applicability of the fundamental freedoms to terms of service that discriminate between consumers in different Member States.

In addition to this (necessary, but rather technical) legal analysis of the case law of the Court, it may be useful to look at the issue from a more practical and political angle. Generally applying the fundamental freedoms of the internal market, in particular the prohibition of discrimination on grounds of nationality in Article 18 TFEU, against private persons would mean obliging private persons to actively contribute to the creation of the Internal Market. This would mean, in particular for businesses active in the DSM, that they are – in principle – obliged to offer their services to all consumers and other customers in the EU or – at least – to provide justification why they restrict their services to certain Member States. In any event, all businesses would be under scrutiny by authorities and courts as to whether their conduct forms arbitrary or justified discrimination. This would be a rather invasive way of improving the DSM which could even deter citizens from starting a business in the DSM.

It is, however, not excluded that there will be cases where the conduct of individual service providers or the conditions in certain market sectors lead to mass discrimination of EU citizens in certain Member States. In cases where the freedom to pursue a trade or profession and the freedom to choose with whom to do business is arbitrarily exercised by businesses and leads to arbitrary discrimination of consumers in certain Member States, the ECJ could (and perhaps should) carefully extend its case law on the horizontal effect of the fundamental freedoms to a horizontally applicable prohibition on discriminating on grounds of nationality in Article 18 (1) TFEU. Such an extension would have to be balanced against the fundamental rights of the private persons concerned and would therefore only be feasible in cases where the increased efficiency of the internal market outweighed the fundamental rights of the affected businesses. In other words: Only in cases where the threat for the internal market justifies the limitation of the fundamental rights of private businesses may the fundamental freedoms and Article 18 (1) TFEU directly apply to those businesses which adversely affect the functioning of the internal market.

As a rule, service providers in the DSM are not obliged under Article 18 (1) TFEU to actively contribute to the creation of the internal market by extending their activities to all Member States, even if there is no justification for not doing so<sup>125</sup>. The exception from this principle are cases where service providers arbitrarily discriminate in such a way that they infringe anti-racism or competition law – or that their conduct puts the internal market at such a risk that limitations in the freedom of service providers to choose with whom to do business is justified for the sake of the DSM.

<sup>124</sup> Cf. Case 44/79 (Hauer) ECR 1979, p. 3727, Paras 31 to 33; Case 265/87 (Schraeder) ECR 1989, p. 2237, Para. 15; Joined cases C-90/90 and C-91/90 (Neu) ECR 1991 Page I-3617, Para. 13.

<sup>125</sup> Cf. A. Epinay, in: C. Calliess, M. Ruffert, EUV/AEUV, 4<sup>th</sup> edition 2011, Art. 18 TFEU, Nr. 44; M. Holoubek, in: J. Schwarze, EU-Kommentar, vol. III, Baden-Baden 2012, Art. 18, Para. 2; Streinz, in: Streinz, EUV/EGV, Art. 12 EC-Treaty, Nr. 39; Zuleeg, EU/EC-Treaty, Art. 12, Nr. 17; M. Rossi, EuR 2000, pp. 216-217.

## 2.5. Fundamental freedoms

As already seen, the fundamental freedoms usually do not defend customers against discriminatory practices of service providers in the internal market. The reason for this is that the protection of fundamental freedoms is principally addressed only to the Member States and the EU. Their purpose is in particular to protect all market participants against prohibitive and protectionist measures of Member States. The fundamental freedoms give market participants the freedom to make use of the internal market. Their purpose is not to force market participants to use this freedom fully. The fundamental freedoms usually do not protect one market participant (e.g. the consumer) from another (e.g. a business which does not want to be active in a certain Member State). The laws which implement the fundamental freedoms, be it in primary or secondary law, are not directed against autonomous decisions of market participants not to make use of the fundamental freedoms. Except for the case of infringement of anti-racism law or of a dominant position which would trigger competition law provisions, service providers in the DSM are not bound by the fundamental freedoms to provide services to market participants in other Member States. The few further exceptions presently formulated by the ECJ concern powerful associations or trade unions, perhaps also individual employers, but not service providers in the DSM<sup>126</sup>.

## 2.6. Prohibition of discrimination by the state in Article 20 (1) Services Directive

*A priori* Article 20 Services Directive appears to form part of the anti-discrimination law of the EU<sup>127</sup> in the same sense as, e.g., the Antiracism or Gender Discrimination<sup>128</sup> Directives. This assumption is, however, incorrect. Article 20 of Services Directive rather aims to achieve a Single Market by the equal treatment of citizens of the Member States who conclude service contracts<sup>129</sup>. Even Article 13 of the Treaty (as well as Article 12; now Article 19 and 18 of the TFEU)<sup>130</sup> has not been mentioned as a source of competence for the Directive.

Article 20 of the Services Directive governs two different issues. In paragraph (1) there is a general prohibition on discriminatory requirements based on nationality<sup>131</sup> or residency<sup>132</sup>. This paragraph is addressed to the Member States and it prohibits rules which would result in discrimination based on these criteria<sup>133</sup>.

For the purposes of this study it has in particular to be analysed to what extent Article 20 (1) is also relevant for discriminatory actions of private businesses. The wording makes clear that only the Member States are addressed. Paragraph (1) requires them to ensure that the recipient is not made subject to discriminatory requirements based on his nationality or place of residence. Taken literally, this phrase would include discriminatory

<sup>126</sup> See above under point 2.4.

<sup>127</sup> L. Roseberry, The Services Directive and the General Principle of Non-Discrimination, in: U. Neergaard, R. Nielsen, L. M. Roseberry, The Services Directive, Copenhagen 2008, p. 121.

<sup>128</sup> Council Directive 2004/113/EC of 13 December 2004 implementing the principle of equal treatment between men and women in the access to and supply of goods and services, Official Journal of the European Communities of 21 December 2000, L 373/37.

<sup>129</sup> C. Herresthal, in: M. Schlachter, C. Ohler, Europäische Dienstleistungsrichtlinie (Services Directive), Baden-Baden 2008, Art. 20 para 2.

<sup>130</sup> On the principle of non-discrimination in accordance with Art. 12 TEU, see M. Rossi, Das Diskriminierungsverbot nach Art. 12 EGV (the principle of non-discrimination in accordance with Art. 12 TEU), EuR 2000, pp. 216.

<sup>131</sup> On the prohibition of discrimination on grounds of nationality see: R. C. A. White, Workers, Establishment, and Services in the European Union, Oxford 2004, pp. 50-51.

<sup>132</sup> C. Herresthal, in: M. Schlachter, C. Ohler, Art. 20 Para. 1, 7.

<sup>133</sup> V. Hatzopoulos, Regulating Services in the European Union, Oxford 2012, p. 259.

practices of private persons which the Member States would have to prevent. Rather hidden in Article 4 (7) of the Services Directive, however, is a substantial limitation of that scope. Article 4 (7) defines the notion of a “requirement” as follows:

*“requirement” means any obligation, prohibition, condition or limit provided for in the laws, regulations or administrative provisions of the Member States or in consequence of case-law, administrative practice, the rules of professional bodies, or the collective rules of professional associations or other professional organisations, adopted in the exercise of their legal autonomy; rules laid down in collective agreements negotiated by the social partners shall not as such be seen as requirements within the meaning of this Directive”;*

This makes very clear that – in principle – only discriminatory practices applied by the state itself or by rules of professional bodies, professional associations or other professional organisations fall into the scope of Article 20 (1) Services Directive – but not any discriminatory practice of other private service providers<sup>134</sup>.

An example of discriminatory behaviour possibly falling within Article 20 (1) of the Services Directive would be the adoption of a road charge only payable by foreign nationals. This example has recently been discussed by German politicians<sup>135</sup>. If the use of public roads were qualified as a service in the sense of the Services Directive, the toll would be an obligation based on the criterion of nationality or residence. As such, the adoption of such a road toll would be prohibited by Article 20 (1) of Services Directive.

In legal writings, there is some dispute as to the precise scope of Article 20 (1) which can be disregarded for the purposes of this study<sup>136</sup>. It may suffice to note that Article 20 (1) only covers discriminatory practices of the state and some professional organisations. This demarcation seems to be inspired by the case law of the ECJ which extended the obligations based on the fundamental freedoms to some professional associations. Any discrimination by the state or these associations based on the nationality or residence of the service providers<sup>137</sup> and clients<sup>138</sup> should be abolished<sup>139</sup>. Article 20 (1) is, however, not applicable to all other service providers.

Article 20 (1) of Services Directive is, moreover, confined to commercial services<sup>140</sup>. All categories of service which are provided for non-commercial purposes, save commercial services provided for free, are excluded. These limitations may have the practical effect that the impact of Article 20 (1) of Services Directive is not wide-ranging. For example, it would be quite difficult to imagine legislative restrictions preventing foreigners from receiving services provided on a commercial basis. Discrimination is more likely to occur in the use of public services which are provided for purposes other than purely commercial ones such as, e.g., health services organised by the state. In these cases, however, Article 20 (1) Services Directive may not apply.

<sup>134</sup> C. Herresthal, in: M. Schlachter, C. Ohler, Art. 20 para 6; V. Hatzopoulos, Regulating..., p. 259.

<sup>135</sup> Equally i.a. Anton Hofreiter (Grüne), Director of the Committee on Transport of the German Parliament, the Bundestag, in the daily newspaper “Rheinische Post” from 05. August 2013, see: <http://derstandard.at/1375626297796/CSU-fordert-Pkw-Maut-fuer-Auslaender> (visited on 13.08.2013).

<sup>136</sup> Cf. D. Parlow, Die EG..., p. 16.

<sup>137</sup> See: the definition of „provider”: R. Streinz, S. Leible, in: M. Schlachter, C. Ohler, Europäische..., Art. 4 Para. 5.

<sup>138</sup> On the benefitting function of the Directive, see: V. Hatzopoulos, Regulating..., p. 259.

<sup>139</sup> D. Parlow argues for the extension of the scope of protection of Article 49 to the recipient, see p. 15.

<sup>140</sup> R. C. A. White, Workers..., p. 50.

## 2.7. Prohibition of discrimination by private actors in Article 20 (2) Services Directive

### 2.7.1. General

Article 20 (2) of the Services Directive was a very innovative approach in secondary legislation, obviously designed as the centrepiece of the protection of consumers against discrimination on grounds of nationality or residence in the single market. However, more than five years after its enactment, the provision seems to have had hardly any effect (if at all) on the single market. The purpose of this subchapter is, firstly, to analyse the content of the provision according to its wording, and secondly, to highlight some of the severe problems of the provision relating to:

- the – partly lacking – legal basis in the Treaty;
- the imminent limitation of the fundamental rights of businesses; and
- the principles of legal certainty and predictability.

In order to analyse the scope of Article 20 (2) of the Services Directive, the following elements must be taken into consideration. Article 20 (2) Services Directive applies:

- to services, as defined in Article 4 (1) of the Directive;
- to any provider, as defined in Article 4 (2) Services Directive, as a party who is an addressee of the duty not to discriminate and
- to every recipient<sup>141</sup>, in the sense of the Article 4 (3) of the Directive, as the person protected against discrimination<sup>142</sup>.

### 2.7.2. The notion of 'service'

The meaning of 'service' in the Services Directive is unclear. Services are defined in Article 4 (1) of the Services Directive. Any self-employed economic activity, usually provided for remuneration<sup>143</sup>, as referred to in Article 57 of the TFEU<sup>144</sup> (former Article 50)<sup>145</sup> falls under this provision. Taken literally this means that services are those activities which are not governed by the provisions of the Treaty related to the freedom of movement of goods<sup>146</sup>, capital and persons. Article 57 of the TFEU explicitly refers to activities of an industrial, commercial and professional character as well as the activities of craftsmen.

The Commission Staff Working Document<sup>147</sup> names the distribution of goods as covered by the Services Directive. This is, however, not supported by the text of the Directive. Since Article 4 (1) of the Directive expressly refers to Article 50 of the Treaty (now Article 57 TFEU), services are those which are not governed by the provisions related to the free movement of goods, capital and persons. In particular, Article 28 of the TFEU distinguishes

<sup>141</sup> C. Herresthal, in: M. Schlachter, C. Ohler, Europäische..., Art. 20 para 5.

<sup>142</sup> The Commission Staff Working Document SWD (2012) 146 final, No. 4.1.5., p. 7-8; On the duties of the provider of services in the Draft Common Frame of Reference, see: M. B. M. Loos, Service Contracts, in: A. S. Hartkamp, M. W. Hesselink, E. H. Hondius and others, Toward a European Civil Code, Nijmegen 2011, pp. 757 (770-775).

<sup>143</sup> D. Parlow, Die EG..., pp. 16-17; R. Streinz, S. Leible, in: M. Schlachter, C. Ohler, Europäische..., Art.4 para 2-3.

<sup>144</sup> On the meaning of Art. 57 TFEU see : V. H.S.E. Robertson, Perspektiven..., pp. 74-75.

<sup>145</sup> D. Parlow, pp. 16-17, On service contracts in the DCFR, see: M. B. M. Loos, Service Contracts, in: A. S. Hartkamp, M. W. Hesselink, E. H. Hondius, pp. 757 (762-770); T. K. Graziano, in: R. Zimmermann, Service Contracts, Tübingen 2010, pp. 59 (74-80); S. Whittaker, in: R. Zimmermann, pp. 115 (132-139).

<sup>146</sup> « Goods » in the sense of the law of the European Union are all tangible movable items, see: C. Herrmann, in : E. Grabitz, M. Hilf, M. Nettesheim, Das Recht der Europäischen Union, 2013, Art. 26 TFEU, Para. 40.

<sup>147</sup> SWD (2012) 146 final, (No. 4.1.1., p. 7); similarly R. Streinz, S. Leible, in: M. Schlachter, C. Ohler, Europäische..., Art. 4 para 2.

the free movement of goods from the free movement of services; this includes all trade in goods. This is so no matter how the contract is formulated or marketed. Contracts concluded on-line concerning goods are covered by Article 28 of the TFEU and are hence not covered by Article 57 of the TFEU. To argue against this position would mean that the fundamental principle of the EU, the free movement of goods, depends on the method of the formation of the contract. It may be true that to a certain extent Article 20 (especially paragraph (2)) of the Services Directive does not fit into the framework of a directive only on services, but to extend the scope of application by analogy would involve going beyond the scope of the directive. Such an extension in the scope of the directive – the subject of negotiation in the legislative process – would probably go beyond the currently accepted rules of interpretation of EU law.

This problem has not yet been properly discussed in legal literature<sup>148</sup>, but it is likely to arise when cases first go to court. The EU legislator should quickly clarify whether the unambiguous wording of its definition of "service" is meant to be taken seriously. If, as Article 4 Nr. 1 of the Services Directive states, "service" means any self-employed economic activity, normally provided for remuneration, as referred to in Article 50 of the Treaty, the scope of Article 20 of the Services Directive would be very narrow. The vast majority of examples where consumers currently experience discrimination would not involve a service and would therefore be outside the scope of the directive.

In the DSM, however, there might, even under the relatively small scope, be some fields of application. Examples could include cloud computing, where the legal qualification of the activity may be disputed with the result that Article 20 (2) may be applicable (despite the exception of Article 2 (c) of the Services Directive). It may be disputed as to whether Article 57 of the TFEU in connection with Article 28 of the TFEU also excludes the sale of digital content. Goods in the sense of Article 28 could be interpreted as tangibles. If this assumption is correct (e.g. the proposal of the regulation on the Common European Sales Law clearly distinguishes between goods and digital content), contracts related to digital content may be regarded as "services" in the sense of the Services Directive.

The distinction between service contracts and sale contracts, however, is very difficult to draw at an abstract level, since there is no general abstract concept of service contracts. The criterion used in the definition of services in the Services Directive by reference to Article 50 (now Article 57 TFEU) may produce numerous difficulties in practice.

It is also extremely difficult to determine whether Article 20 of the Services Directive applies to mixed contracts, consisting of services and obligations which cannot be qualified as services. The law of the European Union (and particularly its primary law) does not contain any typology of contracts. Hence, it is difficult to define whether a mixed contract should rather be treated as a service contract or a non-service contract in the sense of the Services Directive. At least in case of Article 20 of the Services Directive, which is a provision limiting the private autonomy of contracting parties, a narrow interpretation should prevail – only contracts with a dominating services component should be covered.

### 2.7.3. Service provider

A service provider is defined in Article 4 (2) of the Directive as any natural person who is a national of a Member State<sup>149</sup>, or any legal person as referred to in Article 54 of the TFEU (formerly Article 48) and established in a Member State<sup>150</sup>, who offers and

<sup>148</sup> Cf., however Jacob Öberg, *The Services Directive – A Paper Tiger?*, *Europarättslig tidsskrift*, no 1, 2010, at pp. 107-123. Available at SSRN: <http://ssrn.com/abstract=1686995> or <http://dx.doi.org/10.2139/ssrn.1686995>, who only discusses the effect of the directive within the scope of Articles 56 ss TFEU.

<sup>149</sup> L. Roseberry, in: U. Neergaard, R. Nielsen, L. M. Roseberry, p. 121.

<sup>150</sup> D. Parlow, *Die EG...*, pp. 15-16.

provides services<sup>151</sup>. This definition is justified by the general objective of the Services Directive but in the case of Article 20 (2) of Services Directive it is much too narrow. It is not clear why other service providers who are operating outside the European Union, but who are providing services within the EU should not be prevented from discriminating against EU citizens. The notion of a service provider should be given an autonomous definition for the purposes of Article 20 of the Directive. The decisive question is whether the law of the Member States could apply in such circumstances. There would, however, be no justification for allowing discrimination under national law. A natural person who is not an EU citizen, but nevertheless provides services within the European Union should be subjected to the same requirements. That this may not be the case, is a result of the hybrid concept of the directive.

#### 2.7.4. Recipient

Recipient is also defined in Article 4 (3) of Services Directive as a mirror image of the definition of service provider<sup>152</sup>. This definition, which encompasses natural and legal persons, refers to nationality, in case of natural persons, and establishment in a Member State, in case of legal persons. This provision does not protect persons outside of the European Union or even natural persons resident in the EU, but who are not EU nationals. Nevertheless, such persons maybe be protected under the Directive implementing the principle of equal treatment between persons irrespective of racial or ethnic origin which must apply at the very least indirectly to discrimination based on grounds of nationality.

The criteria confining the notion of recipient only to the EU-nationals(in case of natural persons)<sup>153</sup> is not clear. This is a result of the public-law element of the Services Directive which does not target contractual fairness, but rather the functioning of the single market. Nevertheless, despite such an objective, it cannot be denied that any discrimination based on nationality in the area of services provided to the public at large, which is not objectively justified, should also be prohibited.

For the purposes of Article 20 (2) of the Services Directive, it is entirely unclear whether only natural persons or also legal persons are being protected. The reason is that, again taken literally, only natural persons can have a nationality or a residence. The provision can thus only be applied by analogy to legal persons.

The rule in Article 20 (2) does not form a part of consumer law<sup>154</sup>. The recipient may be a professional or non-professional. The notion of the recipient does not concern a real persons. It concerns a standardised description of potential customers from the perspective of access to services.

#### 2.7.5. General conditions of access to a service, which are made available to the public at large

Given its wording, Article 20 (2) of the Services Directive does not oblige the Member States to prevent service providers from actually discriminating against customers. The Member States must only ensure that "the general conditions of access to a service, which are made available to the public at large" do not contain discriminatory provisions. If one takes this literally, service providers would be by no means hindered from discriminating

<sup>151</sup> R. Streinz, S. Leible, in: M. Schlachter, C. Ohler, Europäische..., Art. 4 para 5-13.

<sup>152</sup> D. Parlow, Die EG..., p. 15.

<sup>153</sup> R. Streinz, S. Leible, in: M. Schlachter, C. Ohler, Europäische..., Art. 4 para 14.

<sup>154</sup> According to the Commission Staff Working Document the recipients are mostly consumers (no. 4.1.3, p. 8). Statistically this may probably be correct. But it does not change the conclusion that from a technical point of view the provision in question does not form a part of consumer law. The qualification of the recipient as a consumer does not play a role in the formal application of this rule. This formal criterion is necessary in order to qualify a rule as part of consumer law.



against customers, as long as they did not publicly announce their intentions to discriminate.

It is hardly imaginable that the provision merely aims at hiding any intended discrimination, but does not aim at combating it. By prohibiting the formulation and publication of discriminatory general conditions of access to the service<sup>155</sup>, the directive actually aims at preventing service providers from discriminating. The mechanism of this system is quite sophisticated. It can influence the legal relationship between individuals indirectly. If the service provider actually discriminates, the "non-discriminatory" description of the access could be regarded as misleading information and constitute an infringement of the Unfair Commercial Practices Directive and the national legislation implementing it. It could also mean a violation of pre-contractual information duties and thus trigger various other sanctions of national law. The service provider is thus not directly prevented by this provision from rejecting clients, even if the motivation is discriminatory. By forcing the service provider to abstain from publishing discriminatory conditions of access, the provider is indirectly forced to accept orders from customers from other Member States<sup>156</sup>.

There is some doubt concerning the interpretation of the term "general conditions of access to a service, which are made available to the public at large." The Commission Staff Working Document interprets the term in a rather broad sense<sup>157</sup>. According to the Commission's document the general conditions of access "could also be practices which apply generally without being laid down in publishing information or in documentation made available by the provider, such as information by way of e-mails or letters addressed to service recipients in response to request for information". This interpretation probably goes too far. If there is individual communication with the customer, it cannot be regarded as "general conditions of access made available to the public at large". Individual communication does not mean that the conditions are available "to the public at large". Such doubts as to its precise meaning, however, mainly relate to selecting the right sanction. Discriminatory general conditions made available to the public at large can trigger sanctions under the Services Directive. If the conditions published are not discriminatory, but the service provider actually discriminates, other sanctions, e.g. for misleading advertising under the Unfair Commercial Practices Law, may apply.

#### 2.7.6. Discriminatory provisions relating to the nationality or place of residence of the recipient

Article 20 (2) Services Directive prohibits general conditions differentiating between recipients according to their nationality or place of residence.<sup>158</sup> This formulation creates a number of ambiguities. If the recipient is a natural person and nationality is the ground for discrimination, the provision would only apply to nationalities of the Member States and not every possible nationality<sup>159</sup>. Residency enlarges, but primarily completes this criterion. It only concerns EU-nationals. In addition, this probably only concerns residency within one of the Member States. Discrimination against EU-nationals based on their residency outside of EU-territory would not fall under the scope of application of this provision because it does not adversely affect the functioning of the internal market.

Discrimination based on different locations within one Member State does not fall under the scope of application of Article 20 (2) Services Directive, since it is only an internal affair of

<sup>155</sup> C. Herresthal, in: M. Schlachter, C. Ohler, Europäische..., Art. 20 para 3.

<sup>156</sup> *Contra*: D. Parlow, Die EG..., p. 16.

<sup>157</sup> The Commission Staff Working Document SWD (2012) 146 final, No. 4.1.4, p. 5.

<sup>158</sup> See on the criteria of discrimination: R. C. A. White, pp. 49-60.

<sup>159</sup> D. Parlow, Die EG..., p. 22.



that particular Member State, even if such discrimination may indirectly affect the functioning of the internal market<sup>160</sup>.

The criterion of “residence” is neither established by the Treaties and nor by the Charter of Fundamental Rights. In its Staff Working Document, which is purely explicatory and has no binding force, the Commission indicates that the criterion of residence could be seen as a case of indirect discrimination based on nationality<sup>161</sup>. A similar thought seems to be expressed in Recital (65) of the Services Directive. Although this argument has not been objected to in legal writing until present, it is, in the view of the authors of this study, highly questionable. In numerous decisions, the ECJ has indeed considered discrimination on grounds of residence as indirect discrimination on grounds of nationality. However, as already demonstrated above, nearly all of these cases concern rules in the national legislation of Member States<sup>162</sup> and not activities of private persons.

Moreover, the doctrine of indirect discrimination, as it has been developed by the ECJ and as it is currently formulated, e.g., in Article 2 (b) of the Gender Directive 2004/113/EC (and other anti-discrimination directives), requires that the person who is indirectly discriminated on grounds of, e.g., sex is actually put at a particular disadvantage compared with persons of the other sex. If residence were a criterion for indirect discrimination on grounds of nationality, only those residents in a certain country would be protected who actually have the nationality of that country, but not all other persons (e.g. immigrants, tourists) who have a different nationality. This result would be completely contrary to the purpose of the Services Directive to create an internal market for services irrespective of nationality or residence. As already stated, nationality as such can never be a justifiable reason not to provide a service<sup>163</sup>. Given the purpose of the Services Directive, residence must be seen as an independent criterion which can be applied irrespective of the nationality of the residents. The function of the prohibition of discrimination based on residency aims at protecting the internal market in the whole EU<sup>164</sup>, independent of the nationality of those who are domiciled in a certain Member State.

Although this problem has not yet been properly discussed in legal writing, the authors of this study believe that, when faced with the first cases, the courts will have to take into account when interpreting Article 20 (2) of the Services Directive that a prohibition of discrimination on grounds of “residence” (irrespective of the nationality of the discriminated persons) has no basis in the Treaty.

#### 2.7.7. Directly justified by objective criteria

The basic idea of Article 20 (2) seems to be that only arbitrary discrimination can trigger sanctions whereas any different treatment of customers which is directly justified by objective criteria remains allowed. In other words: Article 20 (2) does not hinder discrimination as such, but only prevents arbitrary discrimination.

Recital (95) of the Directive gives numerous examples of such justifications. For instance, in the context of different tariffs and conditions applying to the provision of a service, such differentiation in tariffs, prices and conditions are justified for objective reasons that can vary from country to country. These include additional costs incurred because of the distance involved or the technical characteristics of the provision of the service, or different

<sup>160</sup> Different: D. Parlow, *Die EG...*, p. 22.

<sup>161</sup> The Commission Staff Working Document SWD (2012) 146 final, No. 4.1.5, p. 9.

<sup>162</sup> See above point 2.4.3.

<sup>163</sup> See above point 2.2.

<sup>164</sup> C. Herresthal, in: M. Schlachter, C. Ohler, Art. 20 para. 2; D. Parlow, *Die EG-Dienstleistungsrichtlinie (Services Directive)*, Hamburg 2010, p. 7.

market conditions, such as higher or lower demand influenced by seasonality, different vacation periods in the Member States and pricing by different competitors, or extra risks linked to rules differing from those of the Member State of establishment. Furthermore, the non-provision of a service to a consumer for lack of the required intellectual property rights in a particular territory would not constitute unlawful discrimination. This list is so long that in the vast majority of cases it should be easy for businesses to find (or to feign) a reason for any refusal to sell or for offering different conditions<sup>165</sup>.

Even for services which are purely digital (such as cloud computing services) different prices can easily be justified by “different market conditions” or the “pricing by different competitors”<sup>166</sup>. It will thus be easy for the provider of music downloads mentioned in the second example in the first chapter<sup>167</sup> to invoke a specific regional reason to justify the practice of providing music tracks for a higher price in some Member States than in others.

If also “higher or lower demand” (without any connection to seasonality) counts as justification, any refusal to sell to a certain Member State can be justified by insufficient demand for even enquiring as to whether there are “rules differing from those of the Member State of establishment” of the service provider. One also wonders whether the pure lack of knowledge of “market conditions” or “pricing by competitors” in another Member State can form a justification for a business not becoming active in that state (or to avoid any cross-border activity and to build up a local distribution structure by, e.g., a subcompany, commercial agents or franchise instead).

Since (regarding “residence”) the basis in the Treaty is lacking and, on the side of the service provider, its fundamental rights from the Treaty and the Charter (including freedom of contract) have to be taken into account when assessing the justification, any economic reason with some trace of plausibility should suffice. The only non-justified discrimination would be a decision not to perform a service on a special territory although it is self-evident that this decision does not have any economic justification – the legal systems do not differ, the language is the same, the cultural conditions are also fully comparable. However, such an ideal situation does not exist even in Austro-German cross-border cases. Hence, practically every justification will satisfy the requirements of Article 20 (2) of Services Directive.

Some businesses fear that further harmonisation of substantial law would take away one of the most evident justifications for not operating Europe-wide which is (in the words of the Services Directive) consumer “rules differing from those of the Member State of establishment” of the service provider. This can be seen in the example of the most ambitious current project, the Common European Sales Law<sup>168</sup>. Since the Common European Sales Law would iron out, or at least reduce, differences of the national laws applicable to the contract, one could draw the conclusion that an e-shop offering to conclude contracts under the Common European Sales Law would no longer be justified in not accepting orders emanating from all Member States. In a very rigid interpretation this could even mean that any e-shop that allows orders to be made under the Common European Sales Law would have to accept orders from customers in all EU Member States. This understanding of the interplay between the Common European Sales Law and Article 20 (2) of the Services Directive would be wrong<sup>169</sup>. The main reason is that the Common European Sales Law is optional. Parties would be entirely free to make use of it or not.

<sup>165</sup> C. Herresthal, in: M. Schlachter, C. Ohler, *Europäische...*, Art. 20 para 21.

<sup>166</sup> See also the Example 3 in the Commission Staff Working Document SWD (2012) 146 final, p. 17.

<sup>167</sup> See: Chapter 1.3.2. of the study.

<sup>168</sup> Proposal for a Regulation of the European Parliament and of the Council on a Common European Sales Law, COM/2011/635.

<sup>169</sup> On this H. Schulte-Nölke, in: R. Schulze, *Common European Sales Law*, 2012, Art. 1 CESL Nr. 5.

Although the Common European Sales Law aims at improving the internal market, its purpose is not to force all businesses that make use of the Common European Sales Law to extend the scope of their commercial activity to the whole territory of the EU<sup>170</sup>.

It is therefore programmatic that Article 1 of the substantial rules of the Common European Sales Law states the principle of Freedom of contract. Read in conjunction with recital (30) of Common European Sales Law<sup>171</sup>, Article 1 could have the function of clarifying that, when using the Common European Sales Law, the parties remain free to limit their activities to a range of certain countries.

Article 20 (2) of Services Directive turns out to be a mainly symbolic provision, expressing the values of the internal market (including freedom of business and freedom of contract). Assuming this as the purpose of the provision, it remains – in principle – left to every service provider to choose his contractual partners freely using criteria he or she considers to be economically favourable. Hence, it is sufficient that the unequal treatment of recipients is economically reasonable. If this justification is accepted, almost every case of discrimination will be justified, because there are always additional risks and costs connected with providing services abroad. This interpretation of Article 20 (2), leaving extensive room for possible justifications, is only conceivable because, in contrast to the discriminations falling under the Anti-Discrimination Directives, the unequal treatment of the recipient is not based on unethical grounds, but solely on the economic reasons of the service provider.

Such purely economic justifications are rather independent from the nature of the service. Delivery or performance abroad can nearly always be said to involve higher costs, make the contract more troublesome to perform and, as the case may be, to enforce or to deal with complaints. This is even true for purely digital services which do not require any physical form of transportation. Taking into account the principle of private autonomy, the decision of whom to contract with is left to each business and must not be interpreted as discriminatory in the sense of Article 20 (2) of the Services Directive.

As already stated, any justification is hardly imaginable in the case of discrimination based on nationality irrespective of the residence of the discriminated persons<sup>172</sup>. Such discrimination will often amount to indirect discrimination on grounds of ethnic origin which is a blatant violation of the law in any case. Article 20 (2), although formally not part of the anti-discrimination law, is misleading to the extent that any discrimination by service providers on grounds of nationality should be prohibited without the possibility of justification.

With respect to residency, the question is much more complex, because it is not sufficiently clear whether this criterion is consistent with the principles of EU law. Traders should generally be free in determining whether they want to provide services in certain territories. Hence, the provision could be read in a manner which only requires an

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<sup>170</sup> Cf also recital (8) of the Common European Sales Law : "To overcome these contract-law-related barriers, parties should have the possibility to agree that their contracts should be governed by a single uniform set of contract law rules with the same meaning and interpretation in all Member States, a Common Sales Law. The Common European Sales Law should represent an additional option increasing the choice available to parties and open to use whenever jointly considered to be helpful in order to facilitate cross-border trade and reduce transaction and opportunity costs as well as other contract-law-related obstacles to cross-border trade. It should become the basis of a contractual relationship only where parties jointly decide to use it."

<sup>171</sup> Recital (3) reads: "Freedom of contract should be the guiding principle underlying the Common European Sales Law. Party autonomy should be restricted only where and to the extent that this is indispensable, in particular for reasons of consumer protection. Where such a necessity exists, the mandatory nature of the rules in question should be clearly indicated."

<sup>172</sup> The Commission Staff Working Document SWD (2012) 146 final, p.11 come (with another line of argument) to the same result.

explanation as to why the scope of the service is being limited only to certain territories of the EU. Only through such a “soft-law” interpretation of Article 20 (2) of Services Directive could the criterion of residency be consistent with the principles of the Treaties<sup>173</sup>. Even in cases where consumer discrimination on grounds of residence in another Member State seems arbitrary and actually affects the internal market, neither primary law nor the Services Directive provide for the means to stop traders from restricting their activity to certain Member States and refusing to accept orders from others. Only competition law may help in such cases.

If, however, Article 20 (2) of the Services Directive is interpreted not as a provision against discriminatory practices, but rather as a provision which aims to foster the economic activity on the internal market and therefore to promote transparency in cross-border transactions, the supplier would have the duty to disclose and to motivate any different treatment of customers from other Member States.

### 2.7.8. Sanctions

Article 20 of Services Directive does not provide sanctions for infringement. The sanctions for the infringement of Article 20 (1) of Services Directive are the same as in the case of every infringement of EU-law by a Member State in cases of the defective implementation of a directive.

Should Article 20 (2) of the Services Directive ever be infringed, sanctions must be provided by the national laws. They can be of a very different nature – e.g. an injunction prohibiting the use of terms and conditions which infringe the directive. In addition, infringements could also be sanctioned as a violation of the collective interests of consumers using the traditional legal mechanisms of public law. Such infringements could also be dealt with by consumer law authorities.

Nevertheless, the question of whether actions which infringe Article 20 (2) of Services Directive may be sanctioned by a right to damages depends very much on the question of what kind of system of liability may be applicable in cases of *culpa in contrahendo*. There is probably no single universal answer to this question. It must, however, be noted that even under quite liberal systems of tort law, it can be quite difficult to satisfy all of the constituent elements for a claim in damages. A claim in damages should result from activities which generally deny access to services or provide different, disadvantageous conditions to access in comparison to persons with other nationalities or places of residence. In many systems the burden of proof in establishing a claim for damages would effectively deprive the claimant of this remedy.

## 2.8. Summary

The anti-racism provisions of the Treaty and in secondary law are usually not infringed by a trader’s refusal to accept orders of consumers from other Member States. The main reason for this is that the anti-discrimination provisions protect the human rights of all natural persons. The frustration of consumers who wish to make use of the internal market does not usually affect their human rights.

The fundamental freedoms **usually do not defend** customers against discriminatory practices in the internal market. The fundamental freedoms give market participants the freedom to make use of the internal market. Their purpose is not to force market participants to use this freedom fully. The fundamental freedoms do not protect one market participant (i.e. the customer) from another (i.e. the business which refuses to sell or only sells **on less favourable terms**). The few exceptions presently formulated by the ECJ

<sup>173</sup> S. Leible, S. Navas Navarro, J. Pisuliński, F. Zoll, in: *Acquis Principles*, Para. 4, p. 159.

concern powerful associations or trade unions, perhaps also individual employers, but not service providers in the DSM. However, the fundamental freedoms constitute an important element when balancing different objectives of EU law, such as e.g. the freedom of businesses to choose whom to do business with or the protection of intellectual property.

Article 18 of the TFEU explicitly contains a directly applicable, autonomous, absolute and general prohibition of discrimination on grounds of nationality and, in paragraph (2), a power allowing for the introduction of further specific prohibitions of discrimination. In cases where the legislation of the Member States made rights or benefits dependent on the residence of persons in a certain Member State, the ECJ has considered this as indirect discrimination on grounds of nationality since such rules are liable to operate mainly to the detriment of nationals of other Member States.

Article 18 TFEU is undoubtedly directly applicable against the Member States and the EU itself. The ECJ has carefully extended the direct applicability of several of the fundamental freedoms to private entities, in particular powerful associations, including trade unions. In a few cases, the free movement of persons has also been directly applied to individual employers. It remains to be seen whether this line of jurisprudence will also be extended to individual service providers in the DSM. Such an extension would have to be balanced against the fundamental rights of the businesses concerned and would therefore only be feasible in cases where improvements in the functioning of the internal market outweigh the fundamental rights of the affected businesses.

Article 20 of Services Directive is a provision which aims at the internal market. Although drafted in the terms of EU anti-discrimination law, it does not form part of it. It is a rule designed to prevent the internal market from disintegrating.

Article 20 (1) of Services Directive prevents the Member States from adopting legislation which inhibits access to services on grounds of nationality or place of residence. This provision of the directive has vertical direct effect. Even if not transposed, a Member State will be seen as infringing EU law if it adopts such discriminatory laws.

Taken literally, Article 20 (2) Services Directive restricts private autonomy. This is partly superfluous, since discrimination based on nationality is already unlawful according to Article 19 of the TFEU. As a person's place of residence is not explicitly mentioned by primary law, it is questionable whether such a limitation on the commercial freedom of businesses may be imposed by secondary law. A service provider should usually have a right to decide where it offers its services since it does not have a duty to contract with every prospective client. The freedom to provide services arising from the Charter of Fundamental Rights operates in two senses – it is also a freedom not to provide services.

It needs to be considered whether at least the part on discrimination based on residency in Article 20 of the Services Directive should be repealed – and not replaced by another potentially oppressive rule, but by further unification of the national laws, diminishing some of the actual obstacles to cross-border commerce in the DSM. The Common European Sales Law and recent ADR/ODR legislation are such steps in the right direction<sup>174</sup>.

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<sup>174</sup> See below under point 3.5.

### 3. PRIVATE INTERNATIONAL LAW - BRUSSELS I AND ROME I

#### KEY FINDINGS

- The current system of international private and procedural law of the EU may, particularly in consumer cases, force the business to litigate abroad and to apply foreign consumer law which is unknown to the business.
- The possibility of litigation with customers, in particular consumers, in foreign courts and, even more, differences in the laws applicable to the contract may form a plausible reason why businesses treat customers from other Member States differently.
- The development of optional instruments with uniform rules and trustworthy ODR schemes may help in overcoming this reason. The current state of the available ODR schemes, however, is far from satisfactory in that regard.

#### 3.1. International procedural law

The core provisions are to be found in Section 4 of Council Regulation 44/2001 on jurisdiction and the recognition and enforcement of judgment in civil and commercial matters (the "Brussels I Regulation"). Section 4 of this regulation derogates from the general rules on jurisdiction in favour of consumers. **In certain situations the consumer is entitled to bring proceedings before the courts of the EU Member State where he has his habitual residence.** Article 15 (1)(c) of the Brussels I Regulation provides the prerequisites under which a consumer may, in his or her national courts, sue a trader with whom he or she concluded a contract, if the trader is resident in another EU Member State. These prerequisites are that:

- the trader pursues commercial or professional activities in the EU Member State of the consumer's habitual residence or, by any means directs such activities to that state, and
- the contract falls within the scope of such activities.

In several recent decisions the European Court of Justice has clarified and to some extent broadened the field of application of this provision<sup>175</sup>. The main dispute was in several cases brought before the court whether a website is "directed" within the meaning of Article 15 (1)(c) of the Brussels Regulation or not. The ECJ provided legal practice with a non-exhaustive list for interpreting whether the trader's activity is directed to the Member State of the consumer's place of residence. Items on this list are:

- the international nature of the activity;
- mention of itineraries from other Member States for going to the place where the trader is established;

<sup>175</sup> Joint Cases C-585/08 and C-144/09 (Pammer/Alpenhof) ECR 2010 I-12527. On the question of whether a seller is obliged to direct his practice to the consumer's place of habitual residence to justify the place of jurisdiction for consumer contracts and concerning the exactly meaning of "directing" requirement, see the pending ECJ case, C-218/12 (Emrek); Opinion of Advocate General's Cruz Villalón of 18 July 2013 (not yet published).



- use of a currency or language other than that generally used in the Member State where the trader is established (in particular the possibility of making and confirming a reservation in another language);
- mention of telephone numbers with an international code;
- outlay of expenditure on an the Internet referencing service in order to facilitate access to the trader's site by consumers domiciled in other Member States;
- use of a top level domain name different from that of the Member State in which the trader is established, or
- mention of an international clientele composed of customers domiciled in various Member States.

It remains, however, for the national courts to assess whether such evidence exists. The result of this case law is that, in particular, e-shops will very often be considered as being "directed" to other Member States. This is the reason why it is likely for businesses to be faced with a competent jurisdiction at the consumer's place of residence, thus being forced to litigate in foreign courts.

In a further recent decision, the European Court of Justice clarified that Article 15 (1)(c) of the Brussels I Regulation does even not require the contract to be concluded at a distance<sup>176</sup>. The ECJ had to decide on a case where an Austrian consumer came across an offer of a German car seller on the Internet and went to Germany to sign the contract and to take delivery of the car. The ECJ held that even in such situation Article 15(1)(c) of the Brussels I Regulation is applicable. The consumer whose car was defect could sue the car seller therefore in her local court in Austria.

### 3.2. Private international law

In B2B cross-border contracts, parties are, in principle, free to choose the applicable law. A party which manages to agree on its own law can therefore escape the need to apply a foreign law. This is of course only true for one of the (at least) two parties in an international contract. Actually, the service provider can 'dictate' a choice of law clause on his business clients under which they either have to accept the applicability of the law of the service provider or to not contract with that service provider at all. The cross border nature of a contract and differences in the contract laws of provider and business customer can therefore hardly form objective criteria which justify different treatment under Article 20 (2) of Services Directive.

In consumer cases (B2C) the situation is, however, different. **Article 6 of the Rome I Regulation** aims to protect consumers in situations where the business pursues its commercial activities in, or directs its activity to, the country of habitual residence of the consumer. If the parties choose a law other than the law of the country of the habitual residence of the consumer, the contract cannot deprive the consumer of the protection afforded by the country of residence. Consumers are therefore always guaranteed the level of consumer protection of their home country. The recent Pammer/Alpenhof case law of the ECJ on the interpretation of "directed activity" in the Brussels I Regulation is most probably also applicable to the issue of whether a website constitutes activities directed to consumers in other Member States.

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<sup>176</sup> Case C-190/11 (Mühlleitner v. Yusufi) ECR (not yet published).



### 3.3. EU legislation and remaining divergences

In the area of contract law there is quite a lot of EU legislation which – however – is still rather patchy and which by far has not led to a great degree of harmonisation.

The E-Commerce Directive only contains some very basic provisions on online contracting, being mainly some specific pre-contractual information requirements.

Other rules are often limited to specific areas of contract law (e.g. pre-contractual information and right of withdrawal in distance and off-premises contracts)<sup>177</sup>, or establish only minimum standards (e.g. unfair terms, consumer sales)<sup>178</sup> where many Member States grant a higher level of protection.

The Common European Sales Law would only be a facultative instrument which indeed could contribute to the solution for the problems posed by the diversity of Member States' laws. Parties would be able to opt-in to a uniform set of rules and thereby remove the need to adapt their contracts to the different laws of the Member States where consumers have their habitual residence. However, given the rather high level of consumer protection in the Common European Sales Law, businesses might be hesitant to make use of the CESL. The CESL could be part of a solution thus, but probably not remove all reasons why businesses decide not to deliver to certain countries.

### 3.4. Recognition and enforcement of judgments

EU Procedural Law, in particular the Brussels I Regulation, also regulates the recognition and enforcement of judgments. It may, however, be questioned whether this area of law is a decisive factor for service providers when considering to offer services in another member state. For consumer cases, jurisdiction is in any case attributed to the country of residence of the consumer. Therefore any judgment against a consumer will be, from the perspective of the state of the consumer's residence, a domestic judgment which should not give rise to any specific problems relating to recognition and enforcement.

This may be different in B2B situations, where, under the current set of EU Procedural Law, jurisdiction may also be attributed to the state where the service provider is established. It is thus rather difficult to assess the extent to which recognition and enforcement issues contribute to or hinder the proper functioning of the internal market and issues of discrimination.

For active litigation (i.e. where the service provider is the plaintiff) the general rule of Article 2 of the Brussels I Regulation would also lead to the jurisdiction of the customer's member state. The same is true for several articles on special jurisdiction. For instance, under Article 5 (1)(a)(b) Brussels I Regulation jurisdiction will, in the case of a sale on goods or the provision of services, lie at the place of performance, which usually will be in the customer's Member State. The enforcement and recognition of judgments are only likely to be relevant in cases where the customer is not a consumer and the service provider manages to reach a valid prorogation of jurisdiction under Article 23 Brussels I Regulation in favour of his local courts. The situation is not very much different for passive litigation (i.e. where the service provider is the defendant). The main difference is that the general place of jurisdiction then is the place of the service provider. Very often, if not even nearly always, there will also be jurisdiction at the place of performance which will, as a rule, be in the customer's country. Since none of these jurisdictions are exclusive, customers are very likely to opt for courts in their own country.

<sup>177</sup> Directive 2011/83/EU (Consumer Rights Directive).

<sup>121</sup> Council Directive 93/13/EEC (Unfair Terms Directive); Directive 1999/44/EC (Consumer Sales Directive).

In general it can thus be stated that service providers, except in the case of a valid prorogation which is only possible in non-consumer cases, will regularly be faced with jurisdiction in the local courts of their customers and are not therefore, or hardly ever, faced with the problem of the recognition and enforcement of judgments.

### **3.5. International private and procedural law as reason for not targeting certain countries**

The critical question is whether the likelihood to be forced to litigate before courts of foreign member states can form a plausible reason for the refusal to sell or any other type of discrimination of customers from certain countries. One could try to find the answer in the field of substantive and not procedural law. The need to negotiate, and if necessary to quarrel, in foreign languages is inherent to nearly any use of the internal market<sup>179</sup>. Hence, the pure fact that litigation in foreign courts would have to be conducted in foreign languages can as such not justify any customer discrimination. The same seems to be true for the need to hire a local lawyer, since this may also be necessary for litigation within the same country. This is merely a consequence of geographical distance, which may, at least within the larger member states, be often as great or even greater for domestic transactions. An example would be a service provider located in the north of Germany which targets the German, Dutch, Danish and Polish markets. Nor can it be assumed that legal services abroad are more expensive than domestic ones<sup>180</sup>. Therefore the main problem would be the application of foreign law, in particular consumer law, to the contract. This may lead to rather unpleasant surprises and costs. Both with regard to psychological obstacles and in terms of costs, it may therefore be concluded as a general rule that the main issue lies in differences in the substantive laws of the Member States, in particular the applicable laws protecting the buyer, customer or consumer in the targeted countries. Since the differences require adapting both, business models and the handling of complaints to local peculiarities, this may form a plausible reason for not providing services in other member states. If the main differences of substantive law, in particular those relating to the rights of customers in case of non-performance or defective performance, were remedied, the remaining risks and costs of litigation in courts of other member states justifying discrimination would crumble away.

### **3.6. Alternative Dispute Resolution (ADR/ODR) as a way forward?**

Very often the development of widely used and effective ADR/ODR schemes is being considered as an important driver for the further development of the internal market. For the purposes of this study the emphasis must lie on the issue of the extent to which effective ADR/ODR schemes can remove reasons which explain consumer discrimination. This question has, in part, already been answered. If it is true, that risks and costs of litigation in foreign courts as such do not constitute a valid reason, ADR/ODR may lower such risks and costs but would probably not change the situation fundamentally with regard to the reasons why the discrimination of consumers from other member states may be justified.

Although logically correct, this conclusion would probably be false under the prevailing market conditions. This may have something to do with costs, but even more to do with psychological reasons. Going to foreign markets is in many respects exposing oneself to the unknown. This is particularly true with regard to court systems and the foreign law.

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<sup>179</sup> The few exceptions, e.g. relations between the United Kingdom and Ireland, France, Luxemburg and parts of Belgium or Germany and Austria left aside.

<sup>180</sup> Example: legal services in Germany are said to be of very high quality and cheaper than most other Member States, cf. the brochure "Law Made in Germany" p. 29, available at: <http://www.lawmadeingermany.de/Law-Made-in-Germany.pdf>.

Although it may be true, that pure differences of court systems are not a valid justification for discrimination, they may nevertheless be an actual reason for doing so. This is ever truer if one assumes that ADR/ODR schemes are more likely to apply uniform detailed rules for dissolving conflicts. Recent empirical studies<sup>181</sup> show that ADR/ODR schemes are not likely to apply highly sophisticated national or international contract law rules. Most of them have a very procedural, sometimes rather simplistic approach in conducting their procedures. This is not only the case for the initial phases in the exchange of forms and negotiation. This is also true when neutrals or computers actively seek to solve the dispute by making proposals for settlement. It is in particular possible, to organise ADR/ODR schemes which nearly completely ignore the applicable provisions of substantive contract law and replace them either by rather basic rules for proposals for settlement of similar disputes or even totally refrain from referring to law and just take the party's expectations into consideration with regard to their BATNAs<sup>182</sup> or WATNAs<sup>183</sup>.

Although such ADR/ODR schemes are rather far removed from a legalistic approach, it is likely that a very high percentage of disputes arising out of service contracts will be solved under them, if run smoothly. There is, of course, always a residual risk of litigation in state courts lurking in the background. If the probability and the total number of cases where ADR/ODR so utterly fails that recourse must be had to the courts can be reduced to a minimum, the risks and costs of litigation in foreign courts become a marginal factor, no longer decisive for the decision of whether to operate in foreign markets or not.

It is therefore correct that **ADR/ODR schemes have a very great potential to remove barriers to the internal market and, importantly in this context, may neutralise objective criteria which justify treating customers differently depending on, in particular, their residence.** Until then, however, there is still a long way to go. Up to present, hardly any ADR/ODR scheme exists which is able to exclude any substantial risk of litigation in foreign courts effectively and consistently. This is not the place to delve deeper into the pre-existing schemes. For the purposes of this study, it is sufficient that even the most common systems, the eBay/PayPal buyer protection schemes, are only applicable for trades on one certain platform where the customer uses a certain means of payment (i.e. PayPal)<sup>184</sup>. It goes without saying and is fully legitimate, that this system, which is run by businesses, may have these limitations in order to market both the platform and the payment system. For many reasons, it may become much more important to improve both, the harmonisation, or unification of substantive law in sectors which are likely to have a particular dynamic for the internal market and to foster the development of ADR/ODR schemes with a sufficiently high penetration of the market in order to instil trust in their smooth operation. Recently enacted EU legislation<sup>185</sup> may be a step towards this direction.

<sup>181</sup> Ch. Hodges, I. Benöhr, N. Creutzfeld-Banda, Consumer ADR in Europe, Civil Justice Systems, 2012.

<sup>182</sup> Best alternative to negotiated agreement.

<sup>183</sup> Worst alternative to negotiated agreement; cf. F. Andrade, P. Novais, D. Carneiro, J. Zeleznikow, J. Neves, Using BATNAs and WATNAs in Online Dispute Resolution, in: New Frontiers in Artificial Intelligence, Lecture Notes in Computer Science Volume 6284, 2010, pp. 5-18.

<sup>184</sup> Cf. <http://pages.ebay.co.uk/help/buy/protection-programs.html>.

<sup>185</sup> Directive 2013/11 EU on consumer ADR; EU Regulation 524/2013 on consumer ODR.

### **3.7. Summary**

Private international law as well as international procedural law very often lead to the result that businesses are forced to litigate in foreign courts and that foreign laws, in particular consumer laws, may be applicable to the contract. Making use of the internal market therefore is exposing oneself to the unknown. This may form a plausible reason not to target certain countries. The harmonisation of substantive law, in particular the development of optional instruments with uniform rules, and the introduction of widespread trustworthy ODR schemes may help in overcoming this reason.

## 4. COMPETITION LAW

### KEY FINDINGS

- Free trade on the DSM may be hindered by anti-competitive behaviours of undertakings creating private barriers. Competition law limits anti-competitive behaviours leading to restrictions on free trade and to market compartmentalisation between Member States.
- Practices which impede competition on the common market will also have similar repercussions for the Digital Single Market. The anti-competitive constraints and infringements resulting from agreements or decisions of undertakings may directly result in implementing territorial restrictions, and affect the availability of goods or services offered to consumers on the Digital Single Market. Exclusive or selective distribution agreements, franchising and agency, as well as vertical and horizontal restrictions, or even rules protecting the intellectual property may restrict the proper functioning of the Digital Single Market.
- Competition law restricts undertakings from creating private market barriers between Member States. Their aims intersect to some extent with aims of the provision of Article 20(2) of Services Directive limiting territorial restrictions of services on the DSM. These rules supplement each other in order to ensure the proper functioning of the internal market.
- The abuse of dominant positions by creating barriers of entry to the market, by market compartmentalisation, or by applying dissimilar conditions to equivalent transactions depending on the nationality or residence of the customers is *prima facie* not allowed under EU competition law.
- To some extent, under block exemptions, competition law allows competition restrictions which restrict consumers' access to goods or services. Furthermore, consumers might be deprived from the ability to purchase certain goods for reasons of safety or health (e.g. some medical products, dangerous substances) or from purchasing goods from a wholesaler (due to separation of retail and wholesale level of distribution).
- The block exemption regulation may result in active sale exclusions. In contrast to active sale exclusions, restrictions of passive sale are generally prohibited. A consumer may not be prevented from purchasing via a website chosen by that particular consumer, nor automatically re-routed to the website of the exclusive distributor without that consumer's knowledge. Nor can a B2C on-line transaction be terminated because of data identified from consumer's credit card or IP address. Restrictions of passive sales, e.g. an on-line sale resulted from a consumer visiting a web site of his or her own accord, or from information delivered to the consumer at his request, are not allowed under European Law.
- Consumers are negatively affected by the lack of information and lack of effective collective redress mechanisms.

### 4.1. Competition Law for the Internal Market - general overview

#### 4.1.1. Primary and secondary sources of the EU competition law

Article 3(1)(b) of the Treaty on the Functioning of the European Union (TFEU) sets out the exclusive competence of the EU to establish provisions of competition law for the

functioning of the internal market. The core primary EU Competition law provisions are **Articles 101, 102 and 106 of the TFEU** (formerly Articles 81, 82 and 86 TEC respectively). Further regulation is to be found in Articles 14, as well as, 103, 104, 105, 119 and 346 of the TFEU.

Secondary sources of EU Competition law provide horizontally and vertically effective provisions to implement and enforce competition rules for the common market. The general framework of competition law is formed by Council Regulation (EC) 1/2003<sup>186</sup> regulating certain aspects of the proceedings for the application of Articles 81 and 82 TEC (101 and 102 of the TFEU), followed by Commission Regulation (EC) 773/2004/EC<sup>187</sup> applied to proceedings conducted by the Commission. **Commission Regulation (EU) 330/2010<sup>188</sup>** defines the category of vertical agreements or concerned practices satisfying the conditions of the block exemptions under Article 101(3) of the TFEU. Further exclusions from Article 101(3) of the TFEU referring to horizontal cooperation agreements are covered by **specific horizontal Regulations<sup>189</sup>**. **Council Regulation (EC) No 139/2004 and the Horizontal Merger Guidelines govern the EU merger control regime.** The unification of the enforcement of Articles 101 and 102 of the TFEU is the subject of Guidance and Notices, which intend to create a set of rules for the consistent application of Articles 101 and 102 throughout the EU<sup>190</sup>.

#### 4.1.2. Scope of application of competition law

Competition law is not applied in legal relations with consumers. Article 101 and Article 102 of the TFEU are addressed to behaviours of undertakings<sup>191</sup>.

The fundamental provision for preventing the competitive market is Article 101 of the TFEU. Article 101 of the TFEU relates to agreements between undertakings, decisions of associations of undertakings and the actions of independent market operators which prevent, restrict or distort competition on the common market. This provision comprehensively covers vertical and horizontal agreements of private and public operators.

Anticompetitive behaviours are generally prohibited under Article 101(1) of the TFEU. On the other hand, certain categories of vertical agreements and other practices recognised as infringing Article 101(1) of the TFEU may be allowed by satisfying the conditions set out in Article 101(3) of the TFEU. These may be permitted even if they imply territorial restrictions, provided that only their efficiency-enhancing results outweigh any anti-competitive effects.

<sup>186</sup> OJ L 1/1, 4.1.2003.

<sup>187</sup> Commission Regulation (EC) 773/2004, consolidated version OJ L 171/3, 1.7.2008.

<sup>188</sup> Commission Regulation (EU) 330/2010, OJ L 102/1, 23.4.2010.

<sup>189</sup> Inter alia: Council Regulation (EEC) 19/65, OJ P 36, 6.3.1965; Commission Regulation (EU) No 330/2010, OJ L 102/1, 23.4.2010; Council Regulation (EEC) 2821/71, OJ L 285, 29.12.1971; Commission Regulation (EU) 1217/2010, OJ L 335/36, 18.12.2010; Commission Regulation (EU) 1218/2010, OJ L 335/43, 18.12.2010; Commission Directive 2002/77/EC, OJ L 249, 17.9.2002.

<sup>190</sup> In particular the European Commission Guidelines on Vertical Restraints, 2010/C 130/01, OJ C 130/1, 19.5.2010 and Communication from the Commission - Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertaking, 2009/C 45/02, OJ C 45/7, 24.2.2009. Others: OJ C 308/6, 20.10.2011; OJ C 101/81, 27.4.2004; OJ C 45/7, 24.2.2009.

<sup>191</sup> In the field of competition law the European Courts adopt the functional concept of undertaking and define it as "every entity engaged in an economic activity, regardless of the legal status of the entity and the way in which it is financed". "Economic activity" must consist in offering goods or services in a given market. Comp. Case C-41/90 (Höfner) ECR I-1979, Para. 21; Case 170/83 (Hydrotherm) ECR 1984 02999, Para. 11; Case C-205/03 (FENIN) ECR 2006 I-6295, Para. 25; Opinion of Advocate General Bot of 4.6.2013 Case C-59/12 (BKK Mobil Oil), Para. 25.

Article 102 of the TFEU applies to undertakings which hold a dominant position on one or more relevant markets. The provision prohibits undertakings from abusing their dominant position within the internal market, in so far as they affect trade between Member States.

#### 4.1.3. Competition law implications of consumers and undertakings on the DSM

Undistorted competition in the common market is one of the main goals of the Treaty. Removing barriers to participation in the market by undertakings enhances market freedoms. The protection of consumers and undertakings encourages market integration, which might be indicated as the factual objective, or end-result, of competition law. Competition law is also ultimately a tool to ensure long-term social welfare<sup>192</sup>.

Articles 101 and 102 of the TFEU and secondary competition law provisions contribute to the protection of effective competition. Competition rules are designed to protect not only the interests of competitors or consumers but to protect the structure of the market and thus competition *per se*<sup>193</sup>. The immediate objective of competition law is the protection of the way in which companies compete<sup>194</sup>.

Competition law is a tool for market integration. The removal of state barriers might be not sufficient, especially if they are replaced with private barriers to trade of goods and services within the common market. Undertakings operating in the common market are prohibited from creating barriers resulting in impediments to trade and dividing the market between Member States. Competition law limits the actions of undertakings which lead to market compartmentalisation.

Actions which impede competition in the common market will operate in similar way in the Digital Single Market. An online distribution might be restricted by exclusive or selective distribution agreements, franchising and agency, as well as vertical and horizontal restrictions, or even rules protecting intellectual property.

Protecting the position of competitors by eliminating anti-competitive behaviours ultimately benefits consumers. Undistorted competition increases the level of consumer safety and confidence by influencing the behaviour of market operators. Effective competition on the DSM benefits consumers through access to a wider choice of goods or services, by eliminating excessive prices and by improving the quality of goods and services<sup>195</sup>. Higher prices and lower quality goods adversely affect consumers. Achieving the goals of competition law is also of major importance from the perspective of consumers.

#### 4.2. Agreements infringing competition and consumers under Article 101(1) of the TFEU

Article 101 (1) of the TFEU prohibits agreements having as their object or effect the prevention, restriction or distortion of competition within the common market. The provision provides for a general ban on agreements between undertakings, or decisions of undertakings or associations of undertakings which impede free competition on the internal market.

<sup>192</sup> R. Nazzini, *The Foundations of European Union Competition Law: The Objective and Principles of Article 102*, Oxford 2011, p. 49.

<sup>193</sup> Comp. Judgment of 14.3.2013, Case T-588/08 (Dole Food) ECR (not yet published), Para. 65.

<sup>194</sup> R. Nazzini, *The Foundations...*, p. 24 -25.

<sup>195</sup> Comp. Judgment of 17.9.2007 Case T-201/04 (Microsoft I) ECR 2007 II-03601, Paras. 643-665.



The purpose of this provision is reflected in the EU case law, according to which agreements perceptibly restricting competition within the common market and capable of affecting trade between Member States are prohibited<sup>196</sup>.

#### 4.2.1. Vertical and horizontal agreements infringing Article 101(1) of the TFEU

Free competition on the DSM is hindered by vertical and horizontal agreements providing for the exclusion of the Internet sales for some types of goods, the forced use of common platforms to distribute supplied products, or fixing higher prices for the Internet sales rather than by traditional sales. **From the consumer's perspective, the distorted access to goods or services means discrimination within the internal market.** As a consequence, this also means that the free movement of goods or services is limited, what is generally prohibited under the Treaty<sup>197</sup>. From the undertaking's perspective, such actions at manufacturers' or distributors' level may improve economic efficiency within the distribution chain and lead to reductions in distribution costs, which may ultimately benefit consumers. Nevertheless, limitations in the choice of products and services, price increases and reductions in the quality of products directly restrict consumers' participation in the market<sup>198</sup>.

Article 101 (1) of the TFEU sets out the general prohibition of vertical and horizontal agreements infringing competition.

The term vertical agreements covers supply and distribution agreements entered into by companies operating at different levels of the production or distribution chain, for instance, agreements between manufacturers of components and producers or between producers and wholesalers or retailers, or between wholesalers and retailers. In distinguishing vertical from horizontal agreements infringing competition, the Court underlined that, while vertical agreements are, by their nature, often less damaging to competition than horizontal agreements, they can, nevertheless, in some cases, also have the potential to be particularly restrictive<sup>199</sup>.

Vertical agreements concluded commonly at different levels of the market chain are considered as typically imposing some restraints on active or passive sales<sup>200</sup>. Gains in efficiency resulting from selective or exclusive distribution systems do not, however, compensate the disadvantages for consumers arising from such anti-competitive practices. Vertical agreements which limit or exclude on-line sale as possible channel of distribution, limit the goods available via the Internet, or operate various territorial restrictions of e-commerce have been the subject of EU proceedings, such as the landmark judgment in case C-439/09 (Pierre Fabre), or in case C-226/11 (Expedia) and case C-108/09 (Ker-optika).

Horizontal agreements are agreements concluded between two or more undertakings operating at the same level of a supply chain. According to the Court, horizontal agreements are, by their nature, often more damaging to competition than vertical

<sup>196</sup> Judgment of 24.10.1995 Case C-70/93 (BMW) ECR 1995 I-03439, Para. 18; Judgment of 28.04.1998 Case C-306/96 (Javico) ECR I-1983, Para. 12.

<sup>197</sup> The non-discrimination principle is broadly expressed by provisions governing market freedoms - see: Services Directive, OJ L 376/36, Recital 95, Article 20.

<sup>198</sup> Comp. EFTA Surveillance Authority Notice - Guidelines on Vertical Restraints 2012/C 362/01, Para. 101.

<sup>199</sup> Joined Cases 56/64 and 58/64 (Consten) ECR 1966 00429; Case 19/77 (Miller) ECR 1978 00131; Case 243/83 (Binon) ECR 1985 -02015; Case C-439/09 (Pierre Fabre) ECR (not yet published).

<sup>200</sup> E.g. the French Competition Authority (*Autorité de la concurrence*) fined pet food manufacturers Royal Canin, Hill's Pet Nutrition, Purina for vertical infringements imposing territorial and customer restrictions, including an absolute prohibition on passive sales. This sales practice resulted in the imposition of an unlawful retail price on end users (consumers).

agreements<sup>201</sup>. Horizontal agreements are considered as practices which jeopardise the proper functioning of the single market and compartmentalise national markets. Horizontal price-fixing, market sharing or output limitations are identified among the most harmful restrictions of competition. Horizontal agreements relating to prices often have as their object the restriction of competition within the meaning of Article 102 of the TFEU<sup>202</sup>. Hence, horizontal agreements or concerted practices between undertakings designed to partition the market are *prima facie* treated as a restriction of competition by object<sup>203</sup>.

#### 4.2.2. Agreements of minor importance not appreciably restricting competition (*de minimis*)

Article 101 (1) of the TFEU does not cover incidental agreements of minor importance which do not appreciably impact trade or competition on common market (the *de minimis* principle)<sup>204</sup>. As a result, even exclusive sales agreements with absolute territorial protection will do not fall under Article 101 (1) of the TFEU, if they do not significantly affect the relevant market<sup>205</sup>.

In order to assess an undertaking's potential to affect competition in the common market the Commission adopted the objective benchmark of the undertaking's market share<sup>206</sup>.

According to the Commission Notice on agreements of minor importance, agreements between undertakings affecting trade between Member States usually do not appreciably restrict competition:

- if the aggregated market share held by actual or potential competing undertakings does not exceed 10 % of relevant market affected by the agreement, or
- if the market share held by each of non-competing parties of the agreement does not exceed 15 % on any of the relevant markets affected by the agreement, or
- in case of restrictions of competition by the cumulative effect of agreements for sales of goods or services by suppliers or distributors of parallel networks, provided that the market share threshold does not exceed 5 %<sup>207</sup>.

Hence, agreements between small and medium undertakings are considered as rarely capable of appreciably affecting trade between Member States<sup>208</sup>, however, they might discriminate against consumers.

Thresholds of market share are not, however, entirely reliable benchmarks. Even agreements which do not reach the thresholds of *de minimis* may constitute an appreciable restriction of competition within the meaning of Article 101(1) of the TFEU and Article 3(2) of Regulation No 1/2003<sup>209</sup>.

<sup>201</sup> Judgment of 14.3.2013 Case C-32/11 (Allianz) ECR (not yet published), Para. 43.

<sup>202</sup> Judgment of 14.3.2013 Case T-588/08 (Dole Food), ECR (not yet published), Para. 415; Judgment of 14.3.2013 Case T-587/08 (Del Monte) ECR (not yet published), Para. 23.

<sup>203</sup> Judgment of 14.3.2013 Case C-32/11 (Allianz) ECR (not yet published), Para. 45.

<sup>204</sup> Commission Notice on agreements of minor importance which do not appreciably restrict competition under Article 81(1) of the Treaty establishing the European Community (*de minimis*), OJ C 368/13, 22.12.2001, Recital 1 and 3.

<sup>205</sup> The relevant market means the relevant product market and the relevant geographic market – see: OJ C 368, 22.12.2001, Recital 10. Comp.: Judgment of 9.4.1969 Case 5/69 (Völk) ECR 1969 I-295, Para. 7; Judgment 6.5.1971 Case 1/71 (Cadillon) ECR 1971 I-351, Para. 9.

<sup>206</sup> OJ C 368, 22.12.2001, Recital 2.

<sup>207</sup> OJ C 368, 22.12.2001, Recital 7.

<sup>208</sup> OJ C 368, 22.12.2001, Recital 3.

<sup>209</sup> Judgment of 6.09.2012 Case C-226/11 (Expedia) ECR (not yet published), Para. 35, 38 and Sentence.

Irrespective of a company's market share, agreements between competing undertakings containing provisions fixing sale prices, limiting outputs or sales, allocating markets or customers are considered as affecting competition.

Agreements between non-competing undertakings may be considered as contrary to Article 101 (1) of the TFEU, even if not exceeding market threshold, where they have as their object imposing fixed prices or limiting the ability of the contracting parties to determine minimum sales prices, or restricting sales to certain Member States or groups of customers. *A contrario* agreements of minor importance (de minimis) not appreciably affecting trade between Member State which do not limit, but restrict active sales into an exclusive territory or to an exclusive suppliers' target group, or restrict sales to end users by a wholesaler, or restrict sales to unauthorised distributors by the members of selective distribution system, might be allowed if they do not appreciably restrict competition<sup>210</sup>. Agreements restricting active or passive sales to consumers by members of selective distribution system operating at a retail level are not, however, permitted<sup>211</sup>.

#### 4.2.3. Assessment of infringements

Various territorial or subjective constraints may result from selective or exclusive distribution agreements based on applying some special standards, requirements or restrictions, inter alia limiting e-commerce<sup>212</sup>. Moreover, certain forms of agreements may by their nature impede the proper functioning of fair competition.

The assessment of existing restrictions created by agreement must refer to the nature of goods and services affected, real conditions of the functioning and the structure of the market<sup>213</sup>.

This also requires taking the characteristics of a distribution channel into account. The nature of the Internet basically excludes the possibility of restricting an undertaking's offer to a specific Member State's territory. The mere fact that the undertaking presents goods or services on its website, combined with a foreign consumer's interest access and the possibility for such a consumer to conclude a contract using the site is not equivalent to actively offering products or services to consumers of that Member States or to specific customers groups. The issue of the website's assessment may, however, be questionable. Activities involving e-commerce of a specific form of product or service, in a language of a specific or narrow territorial coverage may suggest an active sale<sup>214</sup>. In order to avoid discriminating against consumers in the DSM, it is therefore necessary to adopt a precise, and not an extensive understanding, of the term active sale. Conversely, the arbitrary and narrow assessment of passive sales used at retail level will be not applicable.

#### 4.2.4. Infringements by effect and infringements by object

The distinction between 'infringements by effect' and 'infringements by object' seems to be particularly significant for the digital market. The distinction is based on the fact that certain forms of infringement may by their nature very seriously impede the proper

<sup>210</sup> OJ C 368, 22.12.2001, Recital 11 (2)(a-b).

<sup>211</sup> See. OJ C 368, 22.12.2001, Recital 11 (2)(c).

<sup>212</sup> Restrictions on Internet sales were identified in various sectors. The national Competition Authorities intervened against the exclusive distribution of the iPhone through Orange, as well as against restrictions imposed by Bose, or Festina. The Danish company Bang & Olufsen which was banned on December 2012 for prohibiting its distributors from selling its products online (decision available at <http://www.autoritedelaconurrence.fr/pdf/avis/12d23.pdf>).

<sup>213</sup> Judgment of 6.9.2012 Case C-226/11 (Expedia) ECR (not yet published), Para. 21, 36; Judgment 23.11.2006 Case C-238/05 (Asnef) ECR 2006 I-11125, Para. 49.

<sup>214</sup> Comp. moreover criteria of assessment accessibility of the website indicated in the judgement of 7.12.2010 in joined cases C-585/08 (Pammer) and C-144/09 (Alpenhof) ERC 2010 I-12527.

functioning of the market<sup>215</sup>. Even if the concrete effect of an agreement does not affect fair competition on the market, the anti-competitive objective of such an agreement may fall within the scope of Article 101(1) of the TFEU. According to EU case law, even the exchange of information between competitors might infringe competition rules if it reduces or removes the degree of uncertainty as to the operation of the market in question, with the result that competition between undertakings is restricted<sup>216</sup>. The agreement of the nature constituting anti-competitive objects, independently of any concrete effect, may be considered as an appreciable restriction of competition<sup>217</sup>. A typical example of the infringement of Article 101(1) of the TFEU, identified in Case C-226/11 (Expedia), occurred in the context of a bilateral agreement creating joint subsidiary GL Expedia (Agence VSC), concluded between US company Expedia and French public train transport company SNCF. The object of the agreement was to expand the sale of train tickets and travel over the Internet. The newly created joint company provided an expanded offer of online travel agency services via the website voyages-SNCF.com, previously specialised in information on the reservation and sale of train tickets<sup>218</sup>. The partnership between SNCF and Expedia creating Agence VSC was held to be a cartel. The Court judgment emphasised, that 'for the purpose of applying Article 101(1) of the TFEU, there is no need to take account of the concrete effects of an agreement once it appears that it has as its object the prevention, restriction or distortion of competition'<sup>219</sup>.

'Infringements by object' require special attention in the context of e-commerce<sup>220</sup>. The **unlimited and distracted nature of the DSM may often curtain or diminish anti-competitive effects**. The broadly open and digital nature of the DSM facilitates actions which affect the market, but does not make it easy to police them. In Case C-439/09 (Pierre Fabre), the Court considered restrictions of competition by object for the purposes of Article 101(1) of the TFEU caused by a ban on selling goods to consumers via the Internet which was imposed on authorised distributors of a selective distribution network, not covered by the block exemption<sup>221</sup>. The agreement, which created a selective distribution system, provided a contractual clause requiring that the sales of cosmetics and personal care products be made in the presence of qualified pharmacist. The requirement excluded, de facto, the use of the Internet for the sale of such products<sup>222</sup>. The clause was held as restricting competition by object. The object of the agreement prohibiting the Internet sales was the restriction of passive sales to end users wishing to purchase online<sup>223</sup>. The Court stated that neither the prestigious image nor the nature of the litigious cosmetics and personal care products, nor even the block exemption from Article 4(c) of Regulation 2790/1999<sup>224</sup> may legitimise the resulting restriction of competition<sup>225</sup>.

The **exclusion of the Internet as a distribution channel** influences the competitive position of the purchaser, but simultaneously affects consumers by restricting their choice of products available to purchase online. The **extent to which the nature of a product or quality of branding may influence its on-line availability is unclear**. A contractual clause banning the use of the Internet as a means of distribution will generally be

<sup>215</sup> Judgment of 14.3.2013 Case T-588/08 (Dole Food) ECR (not yet published), Para. 69.

<sup>216</sup> Judgment of 4.6.2009 Case C-8/08 (T-Mobile Netherlands) ECR 2009 I-04529, Para. 35, 56.

<sup>217</sup> Judgment of 6.9.2012 Case C-226/11 (Expedia) ECR (not yet published), Para. 37.

<sup>218</sup> Judgment of 6.9.2012 Case C-226/11 (Expedia) ECR (not yet published), Para. 7 and 8.

<sup>219</sup> Judgment of 6.9.2012 Case C-226/11 (Expedia) ECR (not yet published), Para. 35, 38 and Sentence.

<sup>220</sup> See: Judgment of 4.6.2009 Case C-8/08 (T-Mobile) ECR 2009 I-4529, Para. 29.

<sup>221</sup> Case C-439/09 (Pierre Fabre) ECR (not yet published).

<sup>222</sup> Judgment of 13.10.2011 C-439/09 (Pierre Fabre) ECR (not yet published), Para. 13, 14.

<sup>223</sup> Judgment of 13.10.2011 C-439/09 (Pierre Fabre) ECR (not yet published), Para. 47, 54, Sentence.

<sup>224</sup> OJ L 336/21, 29.12.1999.

<sup>225</sup> Judgment of 13.10.2011 C-439/09 (Pierre Fabre) ECR (not yet published), Para. 46.

considered as a restriction by object within the meaning of Article 101(1) of the TFEU, if from the content and objective of that contractual clause, and its legal and economic context, and the properties of the products, it is apparent that the clause is not objectively justified. On-line sales may not lead to lowering the quality of the sale process. Consumers benefit from purchasing online not only by cheaper prices, but also in terms of better services, including inter alia easy access to comprehensive information about the products on offer, the possibility of comparing prices, ordering the products at a distance, as well as by saving time<sup>226</sup>.

Nevertheless, the nature of certain goods or services (e.g. para-medical products, products or substances which can be dangerous to consumers) may justify restrictions of on-line sale, or special requirements of selective distribution, or requirements regarding specific detailed information. In the CIBA Vision Vertriebs GmbH case (CIBA is the German company, leader in the wholesale supply of contact lenses), the German Federal Cartel Office rejected the argument that the restriction of the on-line sale of contact lenses was justified for reasons of consumer health protection<sup>227</sup>. Also the French Competition Authority ordered ten major pharmaceutical companies to offer cosmetic products for sale on the Internet<sup>228</sup>.

### 4.3. Exemptions allowed under Article 101 (3) of the TFEU

Generally anti-competitive conduct or infringements regarding, for example, the Internet sales may be allowed under the block exemption rules. This means that to some extent competition law allows restrictions on competition which disadvantage consumers. The Belgium Supreme Court outlined the sample relationship between EU competition law and unfair competition rules in stating that *"the conduct of an undertaking restricting competition but allowed under antitrust law cannot be prohibited as an act of unfair competition when the alleged violation of honest business practices essentially consist of the restriction of competition"*<sup>229</sup>. The judgment symptomatically reflects the possible model of defining the level of unfairness of commercial practices on the DSM *via* restraints and infringements allowed by the rules of EU competition law.

If an agreement has been found to contravene Article 101(1) of the TFEU, it may nonetheless be purged of its unlawful character by the exemption provided in Article 101(3) of the TFEU. Under Article 101(3) of the TFEU, generally anti-competitive behaviour may be allowed, when it is objectively necessary and proportionate. Conduct which will ultimately lead to oligopolies might be justified whether the efficiencies resulting from competitors' action outweigh any negative effects on competition and consumer welfare and the conduct does not remove all, or most existing sources of actual or potential competition<sup>230</sup>.

<sup>226</sup> Comp. Judgment of 13.10.2011 C-439/09 (Pierre Fabre) ECR (not yet published), Para. 26.

<sup>227</sup> Bundeskartellamt decision of 25.9.2009 in Case B3-123/08 CIBA; furthermore: T. Caspary, Swimming against the Zeitgeist? German Federal Cartel Office issues third fine for resale price maintenance (CIBA), European Competition Law Review 2010, Issue 3. Case C-108/09 (Ker-Optika), ECR 2010 I-12213.

<sup>228</sup> Decision 07-D-07 of 8 March 2007 regarding Bioderma, Caudalie, Cosmétique Active France – L'Oréal, Expanscience, Johnson & Johnson Consumer France, Lierac, Nuxe, Oenobiol, Rogé Cavaillès, Uriage, See: Report L'Autorité de la concurrence 25 Years, 2012, p. 37, available at: [http://www.autoritedelaconcurrence.fr/doc/25years\\_uk.pdf](http://www.autoritedelaconcurrence.fr/doc/25years_uk.pdf).

<sup>229</sup> J. Stuyck, Unfair competition law in the EU in the years to come, in: R. Schulze, H. Schulte-Nölke, European Private Law – Current Status and Perspectives, 2011, p. 129.

<sup>230</sup> Guidance, OJ C 45, 24.2.2009, Recital 30.

The exception provided in Article 101(3) of the TFEU applies where four conditions laid down in this provision are cumulatively satisfied<sup>231</sup>. The exemption from Article 101 (3) of the TFEU shall apply to **agreements, decisions or concerned practices** which:

- result in improving the production or distribution of goods or in promoting technical or economic progress;
- allow consumers a fair share of the resulting benefit;
- do not impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives;
- make it possible for undertakings to eliminate competition in respect of a substantial part of the products in question.

#### 4.3.1. Frames of the block exemptions under the Regulation 330/2010

Vertical agreements falling under the scope of Article 101 (3) of the TFEU may benefit from the block exemption provided *inter alia* by Regulation (EU) No 330/2010 (BER)<sup>232</sup>.

The block exemptions might be applied to vertical agreements for the purchase or sale of goods or services<sup>233</sup>, including vertical agreements containing ancillary provisions on the assignment or use of intellectual property rights<sup>234</sup>. The vital factor determining the applicability of the BER is whether the supplier's and the buyer's market share exceeds 30 %. The Regulation is not applicable to vertical agreements, which may infringe competition and harm consumers.

Article 4 of the BER excludes vertical agreements having as their object resale price maintenance, implementing territorial restrictions, restrictions of passive or active sale to end users, restrictions of cross-supplies, and indicated restrictions of component sale from the ambit of Article 101 (3) of the TFEU (and from the block exemption)<sup>235</sup>. Agreements and practices which restrict the distribution of goods or services by adversely affecting the position of a prospective buyer or its customers, by compartmentalising the market geographically or distinguishing various customer groups are generally considered as hardcore restrictions<sup>236</sup>. Practices requiring the buyer to pay a higher price for products to be exported, limiting products available to customers on the restricted territory, not providing services Union-wide, are excluded from the protection of the BER.

BER protection is not depriving under Article 4(b) for the listed agreements and practices *per se*. The same provisions or practices may be allowed, if they are implemented voluntarily by the buyer, even if they result in territorial restrictions of distributions<sup>237</sup>.

#### 4.3.2. Foreclosure of territorial exclusion of passive sale on the on-line distribution

It is worth mentioning that agreements prohibiting on-line distribution result in restrictions of active and passive sale.

<sup>231</sup> Article 101(3) TFEU can apply to an agreement prohibited under Article 101(1) TFEU only when the undertaking has proved that the four cumulative conditions laid down therein are met.' See: Judgement of 7.2.2013 C-68/12 (Slovenská sporiteľňa) ECR (not yet published), Para. 31, Sentence.

<sup>232</sup> Regulation 330/2010, OJ L 102/1 24.4.2010, Recital 5.

<sup>233</sup> The Regulation 330/2010 does not protect three types of specific restraints, namely non-compete obligations during the contract, non-compete obligations after termination of the contract, the exclusion of specific brands in a selective distribution system. The scope of agreements covered by the block exemption should not be subject of a broad interpretation. See: Judgment of 13.10.2011 C-439/09 (Pierre Fabre) ECR (not yet published), Para. 57.

<sup>234</sup> Regulation 330/2010, OJ L 102/1 24.4.2010, Recital 3.

<sup>235</sup> Regulation 330/2010, OJ L 102/1 24.4.2010, Para. 4 (a)-(e).

<sup>236</sup> Regulation 330/2010, OJ L 102/1 24.4.2010, Para. 4 (b).

<sup>237</sup> SEC/2010/0411 final, Recital 50.



Conducts based on direct or indirect exclusions of selling to certain customers or to customers in certain territories or -often identified in the context of on-line sale- the obligation to refer orders from customers active in one territory to other distributors will be considered as infringing Article 101(1) of the TFEU. However, they may be assessed as corresponding to exceptions from the BER exclusion provided by Article 4(b)(i)-(iv).

Article 4(b)(i) of the BER allows for exclusive distribution agreements restricting an active sale performed by a purchaser to a territory or to a customer group allocated to another buyer or to a supplier<sup>238</sup>. **In contrast to active sale exclusions, restrictions of passive sale are not allowed.** An on-line sale concluded after the consumer visited the seller's website of his or her own accord, or from information delivered to the consumer at his request, is considered a form of passive selling and may be not exempt<sup>239</sup>. The character of the sale remains passive even if an on-line shop facilitates sales to consumers from the territory excluded from its scope of distribution by, for instance, providing different language options, different payments methods, and delivery standards applicable to consumer from different Member States.

Consumers may not be deprived from choosing their distributor, and distributors cannot be restricted in use of the Internet as a method of distribution. The simple marketing of a product or service via distributor's website, which make this product or service available on-line to consumers, is considered as a form of passive sale and, in general, cannot be restricted. The exclusion of the Internet as a means of distribution is compatible with the BER only to the extent allowed by exclusive agreements for active selling<sup>240</sup>.

Pursuant to Article 4(b)(i) of the BER **exclusive distribution agreements may not affect passive sales even provided on territories or to customers allocated to other distributors.** This means that consumers from the territory or consumers group allocated to an exclusive distributor may not be deprived from buying the same goods or services by distributors allocated to another territory or customers group. In this context, agreements imposing systems of automatic re-routing consumers from the chosen website to the website of an exclusive distributor form an unjustified infringement of passive sale, by limiting consumer choice. This is because restricting passive sales are considered as intentional agreements forcing distributors to terminate on-line transaction with consumer from outside the exclusive territory based on credit card data or IP address. Not allowed are, moreover, agreements limiting the amount of an on-line sale based on proportion of on-line sale to sale in mortar shop, which basically result in limiting consumer choice or availability of products offered on-line.

Under Article 4(b) of the BER, three exceptions are, however, allowed from the general prohibition of restricting passive sales. Those which restrict a wholesaler from active and passive selling to consumers are particularly detrimental to consumers<sup>241</sup>.

#### 4.3.3. Assessment of the allowed exemptions

The criteria imposed by vertical agreements on the Internet sales are justified by the nature of this distribution model and equivalent to the criteria imposed on the physical point of sale.

<sup>238</sup> As a consequence, the on-line distributor allocated to other territory or customer groups is not allowed to perform active sales, e.g. direct mailing or target advertising dedicated specifically to consumers in the protected territory. See: BER, para 4 (b)(i).

<sup>239</sup> Guidelines SEC(2010) 411 final, 10.5.2010, Recital 52 and 53.

<sup>240</sup> Guidelines SEC(2010) 411 final, 10.5.2010, Recital 52, 53 and 56.

<sup>241</sup> Guidelines SEC(2010) 411 final, 10.5.2010, Recital 55.



The Guidelines on Vertical Restraints provide vertical agreement self-assessment criteria. The scope of assessment specified in the BER Guidelines covers vertical agreements and concerted practices between undertakings, explicit or implicit in form, as well as the behaviour of undertakings expressing their joint intention, or the tacit acquiescence of one party reflected in the implementation of a unilateral policy and a level of coercion exerted by a party to impose a unilateral policy upon the other party<sup>242</sup>.

The Guidelines seem to allow vertical agreements obliging distributors to sell a certain amount of the products on the Internet to ensure an efficient operation of the physical point of sale<sup>243</sup>. The limitation may artificially lead to providing offers which are less attractive to consumers than offline sale and reducing the potential of the DSM as a platform of goods and services exchange. The obligatory physical point of sale may be justified by requirements of protecting quality standards for online and offline sales, the nature of the products or even in the consumer's interests. Limiting the minimum number of offline sales naturally harms e-commerce as a means of distribution.

Contracts classified as agency agreements are excluded from the scope of Article 101(1) of the TFEU. Agency agreements satisfy the requirements of the block exemption even when they limit the territory of agent's activities, or limit sale to certain customer groups, or fix prices and conditions. The agent's activity is considered as a part of the activities of his principal, which changes the assessment perspective in so far as it allows for the exclusion of the agency agreement from the restrictions of Article 101(1) of the TFEU<sup>244</sup>. In this context, it is also worth mentioning the Case of COMP/39.847/E-BOOKS<sup>245</sup>, where the factual background was that a business forced its distributors to move from a wholesale business model to an agency model, implemented for e-books retailer offering e-books to consumer in the EEA. The Commission found that the joint switching from a wholesale model to the agency model constituted a concerted practice breaching Article 101(1) of the TFEU and Article 53 of the EEA Agreement<sup>246</sup>. Nevertheless, agency agreements may, from their nature, create the context for conduct which discriminates against consumers.

#### 4.4. Discriminatory abuse of dominant position

##### 4.4.1. Implications from consumers' and undertakings' perspective

The dominant position of an undertaking is defined by the cumulative combination of several factors. It is defined "as a position of economic strength held by an undertaking which enables it to prevent effective competition being maintained on the relevant market, by giving it the power to behave to an appreciable extent independently of its competitors, of its customers and ultimately of consumers"<sup>247</sup>. A dominant position may arise from the very large market shares of the undertakings, which put it in a position of strength and makes it an unavoidable trading partner.<sup>248</sup> According to case-law, an undertaking which

<sup>242</sup> Guidelines SEC(2010) 411 final, 10.5.2010, Recital 25.

<sup>243</sup> Guidelines SEC(2010) 411 final, 10.5.2010, Recital 52(c).

<sup>244</sup> Guidelines SEC(2010) 411 final, 10.5.2010, Recital 18.

<sup>245</sup> See: Case IP/12/1367; Case COMP/39.847/E-BOOKS, 2013/C 112/05.

<sup>246</sup> Case COMP/39.847/E-BOOKS, 2013/C 112/05, Recital 4.

<sup>247</sup> Judgment of 14.2.1978 Case 27/76 (United Brands) ERC 1978 00207, Para. 65 and 72; Judgment 15.12.1994 Case C-250/92 (Dansk) ECR 1994 I-5641, Para. 47; Judgment of 23.10.2003 Case T-65/98 (Van den Bergh Foods) ECR 2003 II-4653, Para. 154; Judgment of 22.11.2001 Case T-139/98 (AAMS) ECR 2001 II-3413, Para. 51; Judgment of 2.4.2009 Case C-202/07 (France Télécom) ECR 2009 I-2369, Para. 60; Judgment of 29.3.2012 Case T-336/07 (Telefonica) ECR (not yet published), Para. 147.

<sup>248</sup> Judgment of 23.10.2003 Case T-65/98 (Van den Bergh) ECR 2003 II-4653, Para. 147; Judgment of 24.5.1997 Case 107-76 (Hoffmann-La Roche) ERC 1977 00957, Para. 76; Judgment of 16.7.1998 Case C-264/96 (Imperial Chemical Industries) ERC 1998 I-04695, Para. 148 and 256; Judgment of 2.4.2009 Case C-202/07 (France Télécom) ECR I-2369, Para. 100.

has a market share of 50 % is in, save in exceptional circumstances, a dominant position<sup>249</sup>.

The Treaty does not prohibit undertakings from acquiring a dominant market position or even exercise it, provided that it does not affect trade between Member States.

A dominant undertaking has the potential to influence the production of other undertakings, restricting the availability of resources, limiting market access, offering unfair trading conditions, offering dissimilar conditions to equivalent transactions, creating barriers to entry and eliminating competitors from the market. All these actions limit the level of competitiveness and the freedom of non-dominant undertakings to offer products and services on the market. The dominating undertaking's market strength allows it to impact on the structure of the market, impose purchase or sales conditions and finally to exclude other competitors from the market. As a result, competition is distorted, market integration impaired and consumer choice limited to products and conditions offered by the undertakings with a dominant position. Products or services offered by a dominant undertaking are usually more competitive than products or services offered by high-cost undertaking eliminated from the market. But the offer provided by the dominant undertaking is not necessarily objectively competitive to consumers.

**Consumers benefit from competitive markets.** They are an important interest group benefiting from preventing the abuse of a dominant position. They benefit **through lower prices, better quality, wider choice of goods and services**. The abuse of dominant position on the DSM creates barriers for free consumer access to products and services easily offered *via* distance market channels. The abuse of dominant positions may lead to limits on consumers' access to products and services, charging the consumer with excessively high prices, or imposing unfair contractual conditions<sup>250</sup>.

Consumers benefit from the distance distribution methods and new ITC technologies and solutions, e.g. cloud computing. Unfortunately, increasingly innovative technological solutions make it easier for undertakings to create or abuse their dominant position. Limiting production or technical development deprives consumers of access to innovative products and services, and discriminates against them.

#### 4.4.2. Scope and application of Article 102 of the TFEU

Article 102 of the TFEU refers to situations where because of the presence of a dominant undertaking, the degree of competition is already weakened. The provision prohibits a dominant undertaking from eliminating competitors and strengthening its position by using methods other than those which come within the scope of competition on merits<sup>251</sup>.

Thereby, the provision of Article 102 of the TFEU covers conduct capable of affecting the structure of the market through implementing methods which are different from those governing the normal competition of products or services in commercial transactions<sup>252</sup>.

Article 102 of the TFEU provides a general prohibition of abuse of a dominant position. The activities of a single undertaking or more undertakings which potentially infringe effective and undistorted competition are subject to an assessment under Article 102 of the TFEU.

<sup>249</sup> Judgment of 29.3.2012 Case 336/07 (Telefonica) ECR (not yet published), Para. 150.

<sup>250</sup> Case C-333/94 P (Tetra Pak II) ECR 1996 I-05951; Case C-385/07 P (Der Grüne Punkt), ECR 2009 I-06155.

<sup>251</sup> Judgment of 14.9.2010 Case C-550/07 (AKZO) ECR 2010 I-08301, Para. 70, and Judgment of 2.4.2009 Case C-202/07 P (France Télécom) ECR 2009 I-2369, Para. 106; Case C-457/10 (AstraZeneca) ECR (not yet published), Para. 75.

<sup>252</sup> Case 107/7 (Hoffman-La Roche) ERC 1977 00957, Para. 76, Case 322/81 (Michelin) ERC 1983 03461, Para.111 ; Judgment of 2.4.2009 Case C-202/07 P (France Télécom) ECR 2009 I-2369, Para. 104; Case C-280/08 P (Deutsche Telekom) ECR 2008 I-9555, Para. 174; Judgment of 29.3.2012 Case 336/07 (Telefonica) ECR (not yet published), Para. 170 and 267.

Article 102 of the TFEU applies to behaviour damaging competition structures within the meaning of Article 3(1)(b) of the TFEU, as well as to practices directly harming consumers<sup>253</sup>.

Article 102 of the TFEU provides a non-exhaustive list of practices which abuse a dominant position<sup>254</sup>. The provision enumerates the constitutive elements of an abusive act, evaluated in terms of affecting trade between Member States. The abuse of a dominant position may consist in:

- direct or indirect imposing unfair purchase or selling prices or other unfair trading conditions;
- limiting production, markets or technical development to the prejudice of consumers;
- applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;
- making the conclusion of contracts subject to acceptance by the other parties of supplementary obligations which, by their nature or according to commercial usage, have no connection with the subject of such contracts.

Such a broad approach in listing abusive practices requires a broad concept of anti-competitive abuses, also enforced by the specific assessment of anti-competitive abuse. Rules for an assessment of the impact of the single dominating undertaking are provided under the Guidance issued on 24.2.2009<sup>255</sup>.

Article 102 of the TFEU refers not only to practices damaging consumers directly, but also to those which are detrimental for consumers through the potential impact of a dominant undertaking on effective competition or the structure of the market<sup>256</sup>. Hence, undertakings with a dominant position are obliged to take special responsibility not to hinder free competition<sup>257</sup>.

According to the European case-law an objective concept of “abuse” is adopted. This refers to the conduct of a dominant undertaking which influences the structure of a market and weakens the degree of competition through recourse to methods different from those governing normal competition in products or services on the basis of the transactions of commercial operators and has the effect of hindering the maintenance of the degree of competition still existing in the market or the further competition in the market<sup>258</sup>.

The burden of proof for establishing the abuse of a dominant position rests on the competition authority or claimant. After establishing the anti-competitive behaviour the dominant undertaking bears the burden of substantiating a lawful defence. As a sanction

<sup>253</sup> T. Eilmansberger, How to distinguish good from bad competition under Article 82 EC: in search of clearer and more coherent standards for anti-competitive abuses, *Common Market Law Review* 42: 129–177, 2005, p. 134.

<sup>254</sup> See: Judgment of 29.3.2012 Case T-336/07 (Telefonica) ECR (not yet published), Para 174; Judgment of 17.2.2011 Case C-52/09 (TeliaSonera) ERC 2011 I-00527, Para. 146.

<sup>255</sup> Communication from the Commission - Guidance on the Commission's enforcement priorities in applying Article 82 of the EC Treaty to abusive exclusionary conduct by dominant undertakings, OJ C 45/02, 24.2.2009.

<sup>256</sup> Case 6/72 (Continental Can) ECR 1973 00215, Para. 26; Case C-95/04 P (British Airways) ECR 2007 I-02331, Paras. 103–108.

<sup>257</sup> Article 102 TFEU, OJ C 45, 24.2.2009; see also : Case T-83/91 (Tetra Pak) ECR 1993 II-00755, Para. 114; Judgment of 30.09.2003, T-203/01 (Michelin II) ECR 2003 II-4071, Para. 97; Judgment of 29.3.2012 Case 336/07 (Telefonica) ECR (not yet published), Para. 171 and 270; Judgment of 17.2.2011 Case C-52/09 (TeliaSonera) ERC 2011 I-00527, Para. 24.

<sup>258</sup> Judgments in Case 85/76 (Hoffman-La Roche) ECR 1979 461, Para. 91; Judgment of 3.7.1991 Case C-62/86 (AKZO) ECR 1991 I-3359, Para. 69; Judgment of 17.2.2011 Case C-52/09 (TeliaSonera) ECR 2011 I-527, Para. 27; Case C-457/10 P (AstraZeneca) ECR (not yet published); Para. 74.

for the anticompetitive abuse of a dominating position, the Commission will impose a fine for the purpose of deterrence. In determining the amount of the fine the Commission is to 'take account of the effective economic capacity of offenders to cause significant damage to other operators, in particular consumers and to set the fine at a level which ensures that it has a deterrent effect'<sup>259</sup>.

#### 4.4.3. Practices abusing a dominant position

The abuse of dominant positions may create barriers of entry to the market which take various forms. They may cause impediments resulting from network restrictions, dominant undertaking investments, tariffs or price policies.

Under Article 102 of the TFEU, abuse may consist in price-based exclusionary conduct affecting market uniformity. The provision directly prohibits compartmentalising markets to the prejudice of consumers.

**The anticompetitive abuse of market power resulting in market compartmentalisation** was the subject of Commission proceedings in various cases referring to the telecommunication market. In the proceedings against Deutsche Telekom, the Commission decided that the undertaking abused its dominant position by imposing "unfair prices in the form of a margin squeeze to the detriment of competitors". Deutsche Telekom (applicant) appealed from the Commission's decision. The Court of First Instance (case T-271/03) upheld the Commission's approach, stating that there is a margin squeeze if, given the wholesale and retail prices of the dominant undertaking, an equally efficient competitor would not be able to offer its services other than at a loss<sup>260</sup>. Deutsche Telekom brought an appeal (case C-280/08) against the judgment, stating that the Court failed to take into account the examinations of the margin squeeze made by the German regulatory authority for telecommunications and post. According to the national Authority Deutsche Telekom was not to use an anti-competitive margin squeeze in respect of local loops<sup>261</sup>. In the judgment from 14 October 2010 the Court dismissed the appeal<sup>262</sup>. A similar problem was considered by the Commission in the Case COMP/38.784 (Wanadoo España v. Telefónica). Telefonica applied unfair price tariffs to the supply of wholesale and retail broadband access services on the Spanish market. The Commission fined Telefonica for abuse of a dominant position. In the judgment from 29.3.2012 (case T-336/07), the Court found that the margin squeeze generated by difference between its wholesale and retail charges for broadband access was an anticompetitive abuse of a dominant position on the Spanish broadband access markets<sup>263</sup>.

The current significance of the competitive telecommunication market reflects the Digital Agenda, which is currently one of the Europe 2020 Strategy Flagship Initiatives. The Agenda emphasises the importance of bringing basic broadband to all Europeans by 2013 and seeks to ensure widespread access to much higher the Internet speeds by 2020<sup>264</sup>.

Discrimination against undertakings engaged in intra-EU trade or in favour of domestic undertakings is abusive under Article 102 of the TFEU. The abuse of dominant positions by market partitioning price-discrimination was at the core of the Irish Sugar case<sup>265</sup>, where the Court indicated that determining prices not by supply and demand but by the location

<sup>259</sup> See: Guidelines on the method of setting fines imposed pursuant to Article 23(2)(a) of Regulation No 1/2003, OJ C 210/2, 1.9.2006.

<sup>260</sup> Case T-271/03 (Deutsche Telekom) ECR 2008 II-00477, Paras. 186–194.

<sup>261</sup> OJ 2003 L 263, p. 9.

<sup>262</sup> Case C-280/08 P (Deutsche Telekom) ERC 2010 I-09555.

<sup>263</sup> Judgment of 29.3.2012 Case 336/07 (Telefonica) ECR (not yet published), Para. 167, 178.

<sup>264</sup> COM/2010/0245 f/2, 26.8.2010, p. 19.

<sup>265</sup> Case T-228/97 (Irish Sugar) ERC 1999 II-02969.

of the buyer caused distortion of the competitive process, and excluded foreign producers from the market. Applying dissimilar conditions to equivalent transactions depending on the nationality or residence of the customers is *prima facie* abusive<sup>266</sup>. Discrimination on grounds of nationality or place of residence applies regardless of a specific disadvantage to the person exercising the freedom, which is distinct from the discrimination itself.

The infringement of Article 102 of the TFEU may result from the dominant undertaking's conduct, for instance in the way it provides its services. The European Commission has decided to open an investigation into allegations that Google Inc. has abused a dominant position in online search<sup>267</sup>. The Commission identifies as potentially constituting an abuse of a dominant position the way in which Google's vertical search services are displayed within general search results as compared to services of competitors<sup>268</sup>. Misleading Internet search results deprive consumers from properly assessing the nature and quality of goods and services, their country of origin, and what is of major importance for their price. In this way, the abuse of a dominant position may imperceptibly modify or limit the consumer choice, and discriminate even well informed and reasonably attentive the Internet users<sup>269</sup>.

#### **4.5. Specific types of Restraints and Infringements of competition affecting consumers on the DSM**

Distortions of competition influencing e-commerce affect consumers. From the perspective e-commerce, the anticompetitive driving of suppliers out of the market, collusion between suppliers, limitations of the availability of goods or services to consumers require special attention. Anticompetitive behaviour can be seen in the provision of IT services, e-services including e-payments, postal services, and finally the purchase or storage of goods or digital content.

##### **4.5.1. Refusal to sell or supply**

Consumers compare prices, brands, delivery conditions. The Internet opens the opportunity of access to offers launched by undertakings irrespective of their place of establishment. Unfortunately, consumers are often faced with a refusal to sell because of different contractual terms referring to their place of residence.

The refusal to supply products or services to the consumer may result from exclusive vertical purchasing arrangements between producers and suppliers, or horizontal agreements between undertakings sharing the market between themselves, or from a dominant undertaking limiting the supply of products or services, or purchasing arrangements that exclude a competitor who would be capable of becoming as efficient as the dominant undertaking.

The refusal to sell products and services is *prima facie* considered unlawful. It limits the consumers' access to products and services, and is considered as consumers' discrimination. The restriction of freedom of trade can be seen as the cause of the exclusionary effect<sup>270</sup>. In the joint cases C-468/06 to C-478/06<sup>271</sup>, the Court identified the refusal of a dominant undertaking to meet the orders of an existing customer as

<sup>266</sup> R. Nazzini, *The Foundations...*, p. 200.

<sup>267</sup> The Commission decided on 30 November 2010 to initiate antitrust proceedings in cases COMP/C-3/39.740, COMP/C3/39.775 & COMP/C-3/39.76. The proposed commitments see: [http://ec.europa.eu/competition/antitrust/cases/dec\\_docs/39740/39740\\_8608\\_5.pdf](http://ec.europa.eu/competition/antitrust/cases/dec_docs/39740/39740_8608_5.pdf).

<sup>268</sup> Report from the Commission: Report on competition policy 2012, COM(2013)159 final, 7.5.2013, p. 13.

<sup>269</sup> Case 278/08 (BergSpechte) ECR 2010 I-02517, Para. 35-36; Case C-236/08 (Google France) ECR 2010 I-02417, Para. 89-90.

<sup>270</sup> Case C-95/04 P (British Airways) ERC 2007 I-02331, Para. 69.

<sup>271</sup> Joined cases C-468/06 to C-478/06 (GlaxoSmithKline) ECR 2008 I-07139.

constituting the abuse of a dominant position under Article 82 of the EC, where, without any objective justification, that conduct is liable to eliminate a trading party as a competitor.

A refusal to supply does not reflect *per se* an abuse of a dominant position. A refusal of supply may be legitimate if it is a necessary, proportionate and objectively justified measure to protect the legitimate interests of the dominant undertaking<sup>272</sup>. The notorious example of an anti-competitive refusal to supply in the DSM was result of the abuse of dominant position considered in Microsoft case<sup>273</sup>. The factual background was the refusal to provide computer protocols which would enable the competing operating system vendors to interoperate with Microsoft's Windows operating systems and cooperate with Microsoft's clients. The Microsoft refusal limited the freedom of customers in choosing software provided by other operators.

Conduct which limits the access of new payment service providers to the market might also be assessed from the perspective of freedom of services<sup>274</sup>, as well as competition law. An anticompetitive horizontal agreement based on the refusal to provide financial services may eliminate the competing undertaking from the market. Agreements restricting an e-payment operator provided the factual background to the case C-68/12<sup>275</sup>. The restrictive agreement between three major Slovak banks resulted in terminating their contracts with Akcenta CZ a.s., which was the only Czech non-bank financial institution providing services comprising cashless foreign exchange transactions, competing against traditional banking services and decreasing their profits.

The prohibition of refusal to supply is not absolute. It might be justified by the right of the undertaking to protect its commercial interests.

#### 4.5.2. Distance payment methods

Distance payment methods are of crucial importance for e-commerce transactions. In 2010, 35 billion card payments were made in the European Economic Area (EEA), totalling EUR 1.8 trillion<sup>276</sup>. The selective availability of payment systems, differentiation of fees or contracts conditions, or non-competitive conducts excluding new service providers, ultimately limits consumer access and contribution in the DSM.

Diverse cross-border regimes of payment differentiate between consumers from different Member States in the DSM. Factors mostly influenced consumers payment choices are security, speed and costs of payment<sup>277</sup>, as well as the availability of payment methods to consumer. The existing state of art differentiates consumer position between domestic and cross-border transactions, as well as between e-commerce and traditional transactions. The lack of interoperability of payment services between the Member States affects the free movement of goods, services and payments. A unique and coherent legal framework for e-

<sup>272</sup> I. Grassi, Refusal to Supply and Abuse of Dominant Position in European Antitrust Law: an Analysis of the Case Law of the Court of Justice, Derra, Meyer and Partner Law Firm 2008, p. 415.

<sup>273</sup> See the Commission decision of 27.2.2008 in case COMP/C-3/34.792 Microsoft, as well as the Case T-167/08 (Microsoft) ECR (not yet published).

<sup>274</sup> Directive 2007/64/EC of the European Parliament and of the Council of 13 November 2007 on payment services in the internal market amending Directives 97/7/EC, 2002/65/EC 2005/60/EC and 2006/48/EC and repealing Directive 97/5/EC, OJ L 319/1, 5.12.2007.

<sup>275</sup> Case C-68/12 (Slovenská sporiteľňa) ECR (not yet published).

<sup>276</sup> Report from the Commission: Report on competition policy 2012, COM(2013)159 final, 7.5.2013, p. 5; Judgment of 29.3.2012 Case 336/07 (Telefonica) ECR (not yet published), Para. 149.

<sup>277</sup> COM (2011) 942 final, p. 4 and 12.



payment services is of vital importance. The idea of Regulation (EU) No 260/2012<sup>278</sup> leading to the creation of an integrated market for electronic payments in euro is fundamental to the development of the DSM. The implementation of the standardisation effort allows the Commission to open competition law proceedings in order to ensure interoperability between e-payment schemes throughout EU<sup>279</sup>. Currently pending proceedings intend to investigate whether the e-payments standardisation process undertaken by European Payment Council will not exclude new entrants and payment providers not linked to a banking industry. The process of standardisation of e-payments in the Single Euro Payments Area, undertaken in order to ensure interoperability between current e-payments scheme, requires further the special attention.

Provisions and agreements harmonising interchange fees are to be essential in creating competitive cooperation of European financial institutions. The multilateral interchange fees make up a significant part of the total cost that business must pay for accepting payment cards. The extensive charges and conditions of electronic payments slow down cross-border transactions. They eliminate the usefulness of credit card for micro-payments. In general, the overcharging of distance payment methods discriminates consumers by increasing prices. Bank charges for cross-border payments undermine consumer benefits from online purchase. The inter-bank fees passed on to businesses provoke them to avoid card payments, in favour of cash-payments. Traditional trade often offers consumer discounts for cash payment, unavailable by the Internet transaction. This convinces consumers to choose traditional shopping channels instead of using the Internet.

Proceedings have been brought against MasterCard Incorporated, MasterCard International Incorporated and MasterCard Europe SPRL launched by the Commission. Under Commission Decision C (2007) 6474 of 19.12.2007<sup>280</sup>, the undertaking's conduct was found to have infringed Article 81 TEC and Article 52 of EEA Agreement. The conduct consisted in setting the minimum price (interchange fees) businesses must pay for accepting consumer credit and charge cards for MasterCard and Maestro branded debit cards. The undertakings (applicants) appealed the decision of the Commission before the General Court. The Court in the case T-111/08 upheld the Commission's findings and stated that the setting of inter-charged act fees infringed Article 101 of the TFEU by restricting price competition, which was to the detriment of business and may lead to discrimination of consumers by discouraging the use of the card or by overcharging or discounting for cash<sup>281</sup>.

In 2012, the Commission pursued the new competition law enforcement action against anticompetitive behaviour relating to the multilateral interchange fees (MIFs) charged by credit card companies, in particular Visa's and MasterCard<sup>282</sup>. The significance of the matter steams from the scale of use of the Visa's credit and debit cards, which is approximately 41 % of all payment cards issued in the EEA. The Commission found that the MIF hindered cross-border transactions and maintained the segmentation of the Single Market into national markets.

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<sup>278</sup> Regulation (EU) No 260/2012 of the European Parliament and of the Council of 14 March 2012 establishing technical and business requirements for credit transfers and direct debits in euro and amending Regulation (EC) No 924/2009, OJ L 94/22, 30.3.2012.

<sup>279</sup> Case COMP 39876, see: [http://europa.eu/rapid/press-release\\_IP-11-1076\\_en.htm?locale=en](http://europa.eu/rapid/press-release_IP-11-1076_en.htm?locale=en).

<sup>280</sup> Summary of Commission Decision of 19.12.2007 relating to a proceeding under Article 81 of the EC Treaty and Article 53 of the EEA Agreement (Case COMP/34.579 — MasterCard, Case COMP/36.518 - EuroCommerce, Case COMP/38.580 - Commercial Cards), OJ C 264/8, 6.11.2009.

<sup>281</sup> Case T-111/08 (Master Card) ECR (not yet published), Para. 28, 43, 150, 158. See also pending investigation ref. to interchange fees set by Visa, Ref. No. IP/12/871 and to inter-bank fees set by MasterCard, Ref. No. IP/13/314.

<sup>282</sup> Report from the Commission: Report on competition policy 2012, COM(2013)159 final, 7.5.2013, p. 5.



It appears that the DSM protection requires constant monitoring of the level of national and cross-border e-payment charges.

#### 4.5.3. Price-based practices

Consumers shopping on-line have access to broader offers than in traditional markets. The availability of a wider range of products should result in access to more competitive offers. The main factor encouraging consumers to purchase on-line is lower price. Price savings are a key factor for choosing on e-commerce for 66 % consumers<sup>283</sup>. Hence, agreements disturbing price competition of the DSM are discriminative from the consumers' perspective.

Market practices discriminating against consumers were the subject of proceedings carried out in Case COMP/39.847/E-BOOKS referring to e-books sale<sup>284</sup>. Books Publishers in agreement with Apple Inc. jointly changed from a wholesale business model to an agency model regarding e-book purchase. The adopted agency model<sup>285</sup> was further imposed to other e-books retailer offering e-books to consumer in the EEA. The purchase model was part of a global strategy with the purpose of raising retail prices of e-books or preventing the emergence of lower prices in the EEA for e-books sold in iBookstore. According to the Commission, the joint switching from a wholesale e-book sale model to an agency model, with the same key terms on a global basis, may constitute a concerted practice breaching Article 101 of the TFEU and Article 53 of the EEA Agreement. The barrier created by this anti-competitive conduct had a negative horizontal impact on e-book trade and discriminated against consumers by excluding market-based price competition. As a result of a commitment between the Commission and the Apple and four e-book publishers, the undertakings agreed to terminate existing agency agreements and not to enter into any new agreements containing pricing rules for the next five years<sup>286</sup>. The consumers shall benefit from lower e-book prices unless they are not permitted by a national retail price laws.

Not only practices based on increasing prices, but also price reduction policy, seemingly friendly to consumers, may result in hampering competition, and be evaluated as an exclusionary conduct prohibited under Article 102 of the TFEU. Pricing policy, which leads to foreclosure of equally efficient competitors may consist in reducing prices (e.g. by reducing profits) resulting in losing access of other competitive customers to consumers without incurring financial loss. The ECJ concluded, that prices fixed below the average variable cost must be regarded as abusive since 'a dominant firm has no interest in applying such prices except that of eliminating competitors, and subsequently raise prices by taking advantage'<sup>287</sup>.

Actions exploiting consumers by offering unreasonably high or low prices for goods and services infringe competition and discriminate against consumers. Price based anti-competitive conduct is often considered as price discrimination, understood as offering different prices for the same product to different customers even if costs of sale are the same to each of them<sup>288</sup>. Offering different prices to consumers in different Member States

<sup>283</sup> SEC (2011) 1640, p. 15.

<sup>284</sup> Case IP/12/1367. The Commission accepted the commitments offered by Simon & Schuster, Harper Collins, Hachette, Holtzbrinck and Apple. See: Communication from the Commission published pursuant to Article 27(4) of Council Regulation (EC) No 1/2003 in Case COMP/39.847/E-BOOKS, 2013/C 112/05. Comp. also Report from the Commission: Report on competition policy 2012, COM(2013)159 final, 7.5.2013, p.12-13.

<sup>285</sup> Agency agreement included provisions of so-called most favoured nation clause regarding price grids and the agent's level of commission for consumer sale, 2013/C 112/05, Recital 6.

<sup>286</sup> Report from the Commission: Report on competition policy 2012, COM(2013)159 final, 7.5.2013, p. 13.

<sup>287</sup> Case C-550/07 (AKZO) ECR 2010 I-08301.

<sup>288</sup> R. Posner, Antitrust Law. Second Edition, University of Chicago Press, Chicago and London 2001, p. 79-80.

on DSM may influence the consumer's market position; however from the perspective of competition it is of limited relevance to the analysis of anti-competitive conduct under Article 102 of the TFEU.

#### 4.5.4. Tying and bundling practices

Tying and bundling are common sales practices<sup>289</sup>, which are not usually detrimental to consumers', on the contrary allow them to buy better products at more competitive single prices. Tying might be abusive and infringe competition, however, particularly if it is forced by a dominant undertaking.

The tying practices were considered as infringing Article 102 of the TFEU in the Case T-167/08. The factual background was market practice implemented by Microsoft, which consisted in tying Microsoft Media Player to Microsoft's Windows operating system<sup>290</sup>. In the Microsoft case the Court concluded, that 'inasmuch as tying risks foreclosing competitors, it is immaterial that consumers are not forced to purchase or use WMP. As long as consumers automatically obtain WMP – even if for free – alternative suppliers are at a competitive disadvantage'<sup>291</sup>.

Mixed bundling arrangements that exclude an equally efficient competitor are prima facie abusive under Article 102 of the TFEU. Tying and bundling of products or services may not, however, constitute a violation of Article 102 of the TFEU. These sales techniques may be implemented by every trader and do not require any kind of market power. Regarding online games purchase, where customers are often children, the survey shows that nearly all websites do not inform their users that seemingly 'free of charge' games require further paid purchase of accessories or equipment. Even if such information is provided in game terms and conditions, there is no clear price list. The free game software is linked to the mandatory purchase of add-ons. This practice harms particularly vulnerable consumer groups.

#### 4.6. Summary

The influence of competition infringement into the economic freedom of undertakings and consumer is a constant feature of European court decisions. A strong protection of freedom of trade may be justified not only from economic objectives, but also social goals. Economic links between regions and nations serve to improve social cohesion, cultural exchanges, and stability in international relations. These processes presuppose market integration<sup>292</sup>. Hence, competition law is a tool to create the integrated internal market, and protect it against unjustified compartmentalisation by the agreements and actions of undertakings.

EU Competition law provisions do not prohibit market agreements, practices or decisions of undertakings affecting trade within the common market, where they do not distort or restrict competition in the meaning of Article 101 or 102 of the TFEU. Conduct affecting trade but not infringing effective competition is irrelevant from the perspective of competition law.

Agreements providing restrictions on Internet sales may be allowed under the block exemption provisions if they are objectively justified in terms of efficiency. However, even if agreements restricting an active sale performed by a purchaser to a territory or to a

<sup>289</sup> Tying practices are defined as situation where consumer may buy a chosen product or service only if buys another product. Bundling means exclusive offering products in joint packets of fixed proportions, often offered at a lower price than the same product offered separately. A sample of bundling sale may be sale of group licenses for the software program.

<sup>290</sup> Case T-167/08 (Microsoft) ECR (not yet published).

<sup>291</sup> Judgment of 17.9.2007 Case T-201/04 (Microsoft) ECR 2007 Page II-03601, Para. 833.

<sup>292</sup> Comp. R. Nazzini, *The Foundations...*, p. 28.

consumer group are permitted, agreements restricting passive sales are generally forbidden. Consumers may be not deprived from purchasing via a chosen website, nor automatically re-routed from a website of their choice to the website of an exclusive distributor without their knowledge and consent, or deprived of the ability to purchase on-line based on territory or place of residence (identified by data from credit card or IP address).

The effects of Article 101(1) and 102 of the TFEU interact to some extent with Article 20(2) of Services Directive by limiting territorial restrictions of services in the DSM. On the other hand and despite of their potentially beneficial economic effect, agreements allowed under the block exemption provision implementing restrictions discriminating against consumers based on their territory or place of residence are contrary to Article 20 (2) of Services Directive.

Article 102 of the TFEU applies only to conduct which affects fair competition. The provision requires that a single company's market power does not impair competitive purchasing, trading and providing services in the DSM. The provision particularly and directly protects market competitiveness. Although the Guidance suggests a shift towards a more economic effect-based consumer-oriented approach, it is focused on safeguarding of the competitive process in the internal market and the objectives of Article 102 of the TFEU are not defined satisfactorily from the perspective of the consumer, in particular with regard to discrimination.

Practices impairing competition in the DSM are often difficult to identify, due to market specificity. Failure in identifying the conduct affecting consumers as impeding competition prevents it from being assessed in the light of Article 101 or 102 of the TFEU. As a result, such practices might be left out the remit of competition law provision, despite of their impact in terms of discrimination. To avoid possible protection gaps it seems necessary to ensure uniform measures allowing consumers to report discriminatory practices in the DSM, without identifying their nature or type. Consumers should be informed about existing procedures and solutions serving to submitting notices of violations applicable to them. The process of enhancing consumer knowledge as a tool of indicating single anti-discriminative practices is consistent with the foundations of the new European Consumer Agenda<sup>293</sup>, where it is emphasised that consumers need tools and information to understand their right to complain and actively influence their rights. Consumers are negatively affected by the lack of information and effective collective redress mechanisms.

The comprehensive protection of consumers requires complex and coherent measures. Considering the consumer position seems to be useful in interpreting provisions setting out frames or executing freedom of goods and services, consumer protection, consumer rights, which often overlap fields covered by EU Competition law, and the rethinking of the relationship between EU competition law and the law of unfair competition. The interpretation of competition rules in light of consumer welfare is strongly recommended.

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<sup>293</sup> [http://europa.eu/rapid/press-release\\_IP-12-491\\_en.htm](http://europa.eu/rapid/press-release_IP-12-491_en.htm).

## 5. INTELLECTUAL PROPERTY LAW

### KEY FINDINGS

- Intellectual property rights are not the subject of inviolable and absolute protection. The level of protection of the fundamental right to property, which includes intellectual property, requires balancing with the protection of other fundamental rights.
- The exhaustion doctrine is a legal measure to balance interests which come into conflict with IP rights. This limits IP protection to the level justified by safeguarding specific intellectual property rights. The EU-wide exhaustion doctrine is a measure of avoiding market compartmentalisation and limiting restrictions of distribution.
- The principle of equal treatment justifies applying the exhaustion doctrine to tangible and intangible goods, as well as to services offered on-line.
- Under intellectual property law, right holders may geographically restrict licenses. Therefore intellectual property law allows businesses to compartmentalise the market. Restrictions of passive sale are contrary to the consumers' freedom of access to goods and services on the DSM, and are not permitted under European law.
- Prohibiting geographical restrictions would not require fundamental changes to the international system of intellectual property rights. It would simply ensure that all licences granted for the territory of one Member State are valid for the whole territory of the EU. The tendency to market compartmentalisation is inherent to territorially restricted IP rights.
- The general question posed by the unlimited scope of the digital world is whether, or to what extent, national legal measures serving to protect the intellectual rights of inventors, researchers or authors should be allowed to adversely affect the DSM. The protection of intellectual property rights in the unlimited environment of the DSM requires further harmonisation of national legal measures to achieve a unified system of IP protection.

### 5.1. Intellectual Property Law on the DSM – general overview

#### 5.1.1. Primary and secondary sources of the EU competition law

IP in the EU is governed by primary and secondary legislation at EU level, as well as legislation created at national level. Article 118 of the TFEU grants the EU the competence to establish measures for the creation of European intellectual property rights, to provide for the uniform protection of intellectual property rights throughout the European Union and for the setting up of centralised EU-wide authorisation, coordination and supervision arrangements. The relevant secondary legislation consists of the set of directives harmonising national IP. The core instrument of standardisation of copyrights and related rights is Directive 2001/29/EC (Copyright Directive)<sup>294</sup>, which provides a comprehensive set of measures against infringements of copyright and related rights. Pursuant to Article 1(2)(a) Directive 2001/29, this does not affect existing Community provisions

<sup>294</sup> OJ L 167/10, 22.6.2001.

relating to the legal protection of **computer programs**, which are governed by Directive 2009/24/EC (Software Directive)<sup>295</sup>.

Directive 2004/48/EC<sup>296</sup> on the enforcement of intellectual property rights obliges the Member States to provide for the measures, procedures and remedies necessary to ensure the enforcement of intellectual property rights. Rental and lending rights for authors are established in Directive 92/100/EEC<sup>297</sup>. The legal framework governing trademarks in respect of goods or services is provided under Directive 2008/95<sup>298</sup>. The aim of the Directive is to foster the free movement of goods and services and free competition within the internal market. The procedure for granting a Community Trademark and the rules governing its use are provided by Council Regulation (EC) No 207/2009<sup>299</sup>.

### 5.1.2. IPR scope and implications for DSM

IP rights are not meant to protect consumers. They protect the legitimate economic interests of copyright or patent right holders. The protection of IPR is not, however, absolute. IP is to be balanced with the protection of rights securing different commercial interests, unrelated to the area of IP law, but benefiting from the values secured by IP. Considering the scope of justified measures of IP protection, the Court stated that despite the protection of intellectual property rights in Article 17(2) of the Charter of Fundamental Rights of the European Union, and the protection given to it in the Court's case-law, intellectual property rights are not inviolable and are not the subject of absolute protection. **The level of protection of the fundamental right to property, which includes intellectual property, must be balanced against the protection of other fundamental rights**<sup>300</sup>.

IP rights are protected on the European, as well as at national level. Various provisions of national legal systems, inherently territorial, affect the availability of goods and services protected by IPR on the DSM. Thus, IP protection interferes with the principle of free movement, and consequently affects the benefits which consumers would otherwise reap from the DSM.

## 5.2. Permissible Restraints under Primary Law

The foundations of the DSM are established by provisions of free movement of goods and services and fair competition. IP protection limits both principles. Provisions of intellectual property law protecting the legitimate rights of rights holders (for instance patent holders) clash with the free movement of goods and services. To the extent that IP interferes with the free movement principle, it is also contrary to the non-discriminatory provision of Article 20(2) of Services Directive. Thus, IP protection simultaneously conflicts with rules on competition and discrimination.

According to Article 101(1) of the TFEU, certain agreements distorting competition, which affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition, are prohibited. An exemption from this prohibition is provided under Article 101 (3) of the TFEU and may be declared for agreements promoting technical or economic progress. Commission Regulation 330/2010 provides further clarification of this exemption<sup>301</sup>. Pursuant to Article 2(3) of the Regulation

<sup>295</sup> OJ L 111/16, 5.5.2009. Directive 2009/24 on the legal protection of computer program constitutes *lex specialis* rules in relation to the Directive 2001/29.

<sup>296</sup> OJ L 195/16, 2.6.2004 (OJ 2004 L 157/45 and corrigendum OJ 2004 L 195/16).

<sup>297</sup> OJ L 346/61, 27.11.1992.

<sup>298</sup> OJ L 299/25, 8.11.2008.

<sup>299</sup> OJ L 78/1, 24.3.2009.

<sup>300</sup> Judgment of 29.1.2008 Case C-275/06 (Promusicae) ECR 2008 I-271, Para. 62 to 68.

<sup>301</sup> BER, OJ L 102, 23.4.2010.

the exemption from the restriction of Article 101(1) of the TFEU applies to vertical agreements containing provisions of assignment to, or use by, the buyer of intellectual property rights, provided that these provisions do not constitute the primary object of an agreement. The term intellectual property rights covers, within the meaning of the Regulation, industrial property rights, know-how, copyright and related rights<sup>302</sup>.

License agreements serve as a distinctive example of the way in which IP interferes with competition and non-discrimination law. When IP owners attempt to enforce strict marketing restrictions on their licensees, such agreements clearly restrict free competition, and possibly divide market among licensees, limiting market freedoms. However, by virtue of the exemption from restrictions of Article 101 (1) of the TFEU, license agreements might be not *per se* considered contrary to competition law, despite affecting competition in fact. As a result, license agreements may thus implement territorial restrictions and dividing the market.

### 5.2.1. Some Reflection of Exhaustions Doctrine on DSM

Article 36 of the TFEU (ex. Article 30 TEC) provides the basis for the EU exhaustion doctrine. The exhaustion doctrine, which is a core principle of EU IP law, assumes that once an unrestricted, authorised sale of a patented article occurs (first authorised sale) and the good is placed on the EU market, the patent holder's exclusive rights to control the further movement (use and sale) of that article are exhausted, and the purchaser is free to use or resell that article throughout the EU. Once sold, the IP owner cannot prevent the further distribution of a good, because his IP right is "exhausted". The exhaustion doctrine balances the rights of IP owners and principles of free competition by allowing the IP owner to market the first sale of a product in monopolistic conditions, but then removes the right to the monopoly on further sales of those products which have already been sold. For instance, a wholesaler from EU State X, which sold goods to EU State Y, may not prevent resale (parallel sale) of the sold goods back to State X<sup>303</sup>. The exhaustion doctrine protects the market from perpetual monopolistic and anti-competitive behaviours (like pricing policies, market compartmentalisation) resulting an absolute protection of IPR.

**IP rights are also exhausted by the authorised placing of goods within the EU market** of distributors (also exclusive distributors), agents, licensees, parent companies, related undertakings or subsidiaries of the same group<sup>304</sup>. Therefore, for instance, an exclusive or territorially restricted licence is granted and the licensee sold goods in accordance with the licence agreement to the purchaser, that purchaser may subsequently distribute the licensed goods within the EU, even to territories unavailable to the original licensee.

The IP rights in the majority of goods are exhausted by their first distribution. Article 4 (2) of Directive 2001/29 provides that the distribution right shall not be exhausted within the Community in respect of the original or copies of the work, except where the first sale or other transfer of ownership in the Community is made by the rightholder or with his consent. Directive 2009/24 derogates from the regime of Directive 2001/29 for computer software programs. Article 4(2) of Directive 2009/24 provides exhaustion of rightholder's exclusive rights, by the first authorised intra Community sale of a copy of a software program, with the exception of the right to control further rental of the program or a copy.

The doubtful applicability of the exhaustion rule to services arose with respect to online services. Pursuant to recital 29 of Copyright Directive the exhaustion does not arise in the

<sup>302</sup> BER, OJ L. 102, 23.4.2010, Article 1 (1)(f).

<sup>303</sup> See: Case C-355/96 (Silhouette) ECR 1998 I-04799.

<sup>304</sup> Comp. Case C-2/93 (Ideal Standard) ECR 1994 I-2789, Para. 34.



case of services and on-line services. As a result, every act of online service supply must be authorised where the copyright or related right owner so provides. The previous interpretations restricted the applicability of the exhaustion principle to physical goods, emphasising that online services do not constitute goods, so that exhaustion cannot occur<sup>305</sup>. The current **applicability of exhaustion doctrine unquestionably includes tangible and intangible goods, as well as services.**

The applicability of the exhaustion doctrine to computer programs was considered in Case 128/11 (UsedSoft). The issue was the applicability of the exhaustion doctrine to the right to distribute a copy of a computer program, and whether the contractual exclusion of the transferability of user rights is lawful according to Article 4 (2) of Directive 2009/24<sup>306</sup>. The Court stated that from an economic point of view the sale of a computer program on a CD-ROM or DVD and the supply by downloading from the Internet are analogous, and that an on-line transmission is the functional equivalent of the supply of a tangible medium<sup>307</sup>. Pursuant to Article 4(2) of Directive 2009/24, the 'first sale of a copy of a program' leads to the exhaustion of the right of distribution of that copy. The exhaustion doctrine, pursuant to the principle of equal treatment, therefore covers both, tangible and intangible goods.

Consequently, the exhaustion rule promotes the free movement of goods, as well as services protected by IP. The exhaustion applies to the distribution of tangible mediums of holding digital property and digital goods transferred from the Internet, including those downloaded from a cloud environment. The logic of the UsedSoft judgment seems to be, moreover, applicable to various forms of digital content protected by IP rights, for instance e-books, e-journals, music<sup>308</sup>.

### 5.3. Sector-Specific Exemptions on Exhaustion

Some exclusion from exhaustion may result from sector-specific exemptions rules. The strict effect of territorial exhaustion is based on the lack of the rightholder's consent necessary to transfer the ownership of the original or copy of the work, which is required for exhaustion. As a result, this excludes the exhaustion of IP rights in the territory covered by restriction<sup>309</sup> and also restricts a direct or subsequent distribution outside the licensed territory.

The specific block exemption regulations are provided for various agreements. Sector-specific exemptions may apply to R&D agreements, specialisation agreements and technology transfer agreements<sup>310</sup>. The two main types of BER dealing with IP relate to technology transfer agreements<sup>311</sup> and agreements for research and development<sup>312</sup>.

The Commission Regulation (EC) 772/2004 (TTBER)<sup>313</sup> provides a block exemption on technology transfer agreements between undertakings (licensor and licensee). The

<sup>305</sup> Comp. G. Westkamp, Intellectual Property, Competition Rules, and the Emerging Internal Market : some thoughts on the European Exhaustion Doctrine, *Marquette Intellectual Property Law Review* 2007, vol. 11, p.320.

<sup>306</sup> See: R. M. Hilty, K. Köklü, F. Hafenbrädl, Software Agreements: Stocktaking and Outlook - Lessons from the UsedSoft v. Oracle Case from a Comparative Law Perspective, *Munich* 2013, MPI IIC (2013) 44, pp. 272-274.

<sup>307</sup> Judgment 3.7.2012 Case C-128/11 (UsedSoft) ECR (not yet published), Para. 61.

<sup>308</sup> Likewise: Opinion of Advocate General Kokott in the Case C-429/08 (Karen Murphy v. Media Protection Services Ltd.), Paras. 175, 185, see also: R. M. Hilty, K. Köklü, F. Hafenbrädl, *Software...*, p. 284, 290.

<sup>309</sup> Comp. G. Westkamp, *Intellectual Property...*, p. 310.

<sup>310</sup> [http://www.wipo.int/edocs/mdocs/mdocs/en/cdip\\_4/cdip\\_4\\_4\\_rev\\_study\\_inf\\_4.pdf](http://www.wipo.int/edocs/mdocs/mdocs/en/cdip_4/cdip_4_4_rev_study_inf_4.pdf).

<sup>311</sup> See: L. Peepkor, L. Kjolbye, The New Technology Transfer Block Exemption Regulation and Guidelines, 2005, <http://www.eui.eu/RSCAS/Research/Competition/2005/200510-CompPeepkor&Kjolbye.pdf>.

<sup>312</sup> Commission Regulation (EC) No 2659/2000 of 29 November 2000 on the application of Article 81(3) of the Treaty to categories of research and development agreements, OJ L 304/7, 5.12.2000.

<sup>313</sup> OJ L 123/11, 27.4.2004.



exemption may cover the transfer of a patent and their application, design rights and know-how, as well as software copyright. The TTBER may be not applied to other copyrights or trademarks licensing<sup>314</sup>. Article 2 of the Regulation establishes the general scope of exemptions, which are limited to agreements satisfying conditions provided in Article 101 (3) of the TFEU, as well as technology transfer agreements that do not constitute the primary object of such agreements, but are directly related to the application of the licensed technology. The Regulation does not define the technology transfer agreements which are capable of falling within Article 101 (1) of the TFEU. The application of the exemption from Article 101 (3) of the TFEU requires an individual assessment of every agreement. The assessment requires taking into account various factors, in particular the structure and the dynamics of the technology and product markets.

The technology transfer agreements may cover various forms of agreements relating to the DSM. Among them are patent licensing agreements, software copyright licensing agreements, as well as agreements containing provisions which relate to the sale and purchase of products or which relate to the licensing of other intellectual property rights or the assignment of intellectual property rights. The technology transfer block exemptions may result in the emergence of monopolies.

The block exemption may apply to agreements, which do not either contain hardcore restrictions provided in Articles 4 and 5 of TTBER or affect competition within the meaning of Article 101 (1) of the TFEU. The TTBER generally excludes territorial restrictions<sup>315</sup>.

Exemption rules impact on market freedoms by creating market or territory restrictions. The exemption affects the product market, which under Article 3 of TTBER is understood as "goods and service markets in both their geographic and product dimension"<sup>316</sup>. The exemption may therefore cover more than one level of trade agreement providing for the setting up of a particular distribution system and specifying the obligations the licensee must or may impose on resellers of the products produced under the licence. Nevertheless, agreement must not infringe competition rules applicable to supply and distribution agreements<sup>317</sup>.

The notion of 'exclusive territory' under Regulation 772/2004 should not be equated with the territory of a Member State. According to the definition of Article 1 (I) 'exclusive territory' means a territory in which the undertaking exploits the invention. The definition abstracts from the territory in the geographical meaning. Its application to the digital market is possibly confusing.

### 5.3.1. Exclusion from block exemptions

Article 4 and 5 of TTBER provide hardcore restrictions of competition excluding licensing agreements from TTBER benefits.

Article 4(1)(c), referring to agreements between competitors, as well as Article 4(2)(b) referring to non-competitors, both generally exclude the allocation of markets or customers. Subsequently, both allow some exclusive territorial and exclusive customer group restriction.

Pursuant to Article 4 (1) of TTBER, the exemption from Article 2 shall not apply if the non-reciprocal agreement concluded between competing undertakings brings about a restriction

<sup>314</sup> Commission Notice - Guidelines on the application of Article 81 of the EC Treaty to technology transfer agreements (TTBER), OJ L. 101/02, 27.4.2004, Recital 52, 53.

<sup>315</sup> OJ L. 123/11, 27.4.2004, Recital 9, Article 2.

<sup>316</sup> OJ L. 101/02, 27.4.2004, Recital 20.

<sup>317</sup> OJ L. 123/11, 27.4.2004, Recital 19.

of active or passive sales by the licensee or the licensor. *A contrario*, the **block exemption does not apply if the reciprocal agreement restricts an active or passive sale on the basis of the territory or customer group**.

Pursuant to Article 4 (2) of TTBER, agreements concluded between non-competing undertakings are exempt if they provide for a restriction based on the territory or customers to whom the licensee may passively sell the products involved. However, Article 4 (2) (b)(i-ii) and (c) of TTBER specify types of agreements between non-competing parties which may **restrict passive sales into an exclusive territory or to an exclusive customer group** reserved for the licensor or allocated by the licensor to another licensee during the first two years that another licensee sells the same products in that territory or to that customer group, as well as agreements which may restrict an active or passive sales to end-users by a licensee which is a member of a selective distribution system and which operate at the retail level.

The aforementioned restrictions form exceptions from the general prohibition of restricting passive sale within the UE territory. Nevertheless, IP rules allow for the restriction of consumers' access to goods protected by IP rights and the compartmentalising the Internal Market.

The hardcore restriction for licensing concerns, moreover, the fixing of prices for products sold to third parties (competition restrictions by object)<sup>318</sup>. Agreements restricting competition by price modelling are mostly excluded from the TTBER. Competitors' agreements are considered as anti-competitive if they e.g. fix minimum, maximum or recommended prices, in a form of an exact price or price list or agreements, where royalties are calculated on the basis of all product sales irrespective the application of the licensed technology<sup>319</sup>. However, an agreement of non-competitors may fix a maximum sale price or recommend a sale price, provided that it does not amount to a fixed or minimum sale price<sup>320</sup>.

Article 6 (2) of TTBER provides for the right of the competition authority of the Member State to withdraw the exemption, where the technology transfer agreement to which the exemption applies has effects which are incompatible with Article 81(3) of the Treaty (Article 101 (3) of the TFEU) in the territory of a Member State, or in a part thereof, which has all the characteristics of a distinct geographic market. The withdrawal is applicable pursuant to Article 29(2) of Regulation (EC) No 1/2003, in respect of that territory.

#### 5.4. Territorial restraints and national provisions

Since IP rules at national level are necessarily territorial, such rules do, to a certain extent, create specific national market restrictions. The protection of IP by specific territorial restraints intersects with the principles of the free movement of goods and services and a harmonised EU IP.

Article 36 of the TFEU identifies the conflict between free movement of goods and services and intellectual property protection. Pursuant to Article 36 of the TFEU, the protection of industrial and commercial property may justify prohibitions or quantitative restrictions of the import and export of goods in transit. **To a certain extent, the Treaty prioritises IP protection over the free movement of goods**. However, the Treaty actually only restricts the level of the interaction of IP with market freedoms. **Arbitrary discrimination and distinguished restriction on trade between Member States**, mentioned in Article

<sup>318</sup> OJ L 123/11, 27.4.2004, Article 4(1)(a) and 4(2)(a).

<sup>319</sup> OJ L 101/02, 27.4.2004, Recital 79 to 81.

<sup>320</sup> OJ L 123/11, 27.4.2004, Article 4(2)(a).

36 of the TFEU, **designate the boundaries of this priority**. The Treaty thus prohibits discrimination based on grounds of nationality.

#### 5.4.1. Copyrights protection

Pursuant to Article 4 (1) of Copyright Directive, Member States shall provide authors with the exclusive right to authorise or prohibit any form of distribution to the public, by sale or otherwise. The protection of copyright, due to its universal nature, is in a certain sense less territorial than the protection of registered patents or trademarks. Despite its harmonisation, some differences in the application or enforcement of copyrights provisions may arise at national level. This will result in territorial discrepancies between the availability of goods or services, supply conditions and prices. In this way, national rules protecting copyright interact with the free movement of goods and services<sup>321</sup>.

The application of national rules was the factual background in the case C-70/2010. Considering the legal and factual grounds of the refusal to install a system for filtering electronic communications, the Court stated that national rules which provide for such measures shall not create barriers to legitimate trade<sup>322</sup>. All measures provided by the national legislators must also be fair and proportionate and not excessively costly<sup>323</sup>.

Provided measures strike a balance between the rights of protected parties and the rights of entities affected by these measures, such like the freedom to conduct business. Disproportionate measures are classified as seriously infringing the freedom to conduct business. However, the fundamental rights of customers of parties affected by these measures may not be infringed<sup>324</sup>.

#### 5.4.2. Territorial trademarks protection

The product and service trademark may be protected at national level by a territorially restricted trademark, as well as European-wide by a community trademark. Article 5 (1) of Directive 2008/95 provides trademark owners with the exclusive right to their trademarks and contains protection against the use by third parties of signs which are identical to any given trademark in relation to identical goods or services. Member States may provide that the absolute protection of trademarks be extended in the course of trade to any sign which is identical with, or similar to, the trademark in relation to goods or services which are not similar to those for which the trademark is registered, if the trademark is well-known in the Member State and the use of the sign takes unfair advantage or is detrimental to the trademark<sup>325</sup>. Despite the broad scope of the protection given to the owner of the trademark, it is to be concluded from the European case-law that the exercise of the exclusive right conferred by the trademark must be reserved to cases in which a third party's use of the sign adversely affects, or is liable to adversely affect, the functions of the trademark, particularly its essential function of guaranteeing the origin of the goods to consumers<sup>326</sup>.

Article 5 (1) of Directive 2008/95 might be analysed from the perspective of trademark protection, and from the perspective of market and consumer protection. Pursuant to Recital 7 of the Preamble of Directive 2008/95, the provisions of the Directive should not exclude the application to trademark provisions of the law of the Member States relating to

<sup>321</sup> See: D. T. Keeling, *Intellectual Property Rights in EU Law Volume I: Free Movement and Competition Law*, Oxford 2004, p. 266.

<sup>322</sup> OJ L. 195/16, 2.6.2004, Article 3.

<sup>323</sup> OJ L. 195/16, 2.6.2004 Article 3; see also: Case T-240/11 (L'Oreal), Para. 139.

<sup>324</sup> Judgment of 24.11.2011 Case C-70/10 (Scarlet), Para. 45 to 50.

<sup>325</sup> Article 5 (2) Directive 2008/95, OJ L. 299/25, 8.11.2008.

<sup>326</sup> Judgment of 22.09.2011 Case C-323/09 (Interflora) ECR 2011 I-08625, Para. 1.

unfair competition, civil liability or consumer protection<sup>327</sup>. **Disparities between national provisions**, despite the current level of harmonisation, may result in unjustified obstacles to, and territorial restrictions of, trade on the common market.

Registration of a community trademark may not result in prohibiting third parties from using the trade mark where it is necessary to indicate the intended purpose of a product or service. The owner of a trademark registered in an EU Member State or a community trademark is, however, allowed, by virtue of the exclusive right conferred by the trademark, to prevent online sales to a consumer located in a territory covered by the trademark made without the consent of the trademark owner.

Article 5 (3) of Directive 2008/95 provides restrictions serving to protect trademarks against infringement, which may arise by offering the trademark protected product in other Member States. The infringement may arise from offering a trade-marked product via the Internet to consumers in the territory of another Member States covered by the registered trademark. In the Case C-324/09 (L’Oreal) the Court emphasised, that the territorial protection of intellectual property in the information society, pursued by Directive 2004/48, allowed Member States to take measures against infringements committed through on-line distribution<sup>328</sup>. To determine whether the protected product is offered in the territory covered by the trademark, it is not sufficient to observe that a website, on which the product is offered, is displayed and accessible in the territory of that particular Member State. **Website accessibility in a technical sense does not alone infringe a trademark**. It cannot be concluded from the specificity of the Internet environment that website accessibility from the territory covered by the trademark means targeting consumers in that territory.

Marketing of goods with a sign identical to a registered mark and the selection of this sign as a referencing word in the Internet search engine may mislead consumers<sup>329</sup> and lead to violations of economic interest of the trademark owner. Hence, the EU law allows the owner of the trademark to prohibit the Internet advertising based on a keyword identical with a trademark reference keyword, which is selected in an the Internet referencing service, if this use adversely affects the functioning of the trademark<sup>330</sup>. This will protect consumers against misleading advertising. The negative impact on the legally protected trademark will be considered if the Internet advertisement would mislead the reasonably well-informed and reasonably observant Internet user, and make it difficult to identify the place of origin of the product<sup>331</sup>.

## 5.5. Summary

Intellectual property rights are not the subject of inviolable and absolute protection. The level of protection of the fundamental right to property, which includes intellectual property, requires balancing its protection with that of other fundamental rights. The interface between IP protection and market freedoms, or competition law, reveals various restraints resulting from IPR.

The exhaustion doctrine is a legal measure for the balancing of IP rights. The **exhaustion limits IP protection to the level justified by safeguarding specific intellectual property rights**. The objective of the exhaustion doctrine, which is considered as a core part of EU law, is to avoid market compartmentalization and limitation of restrictions of

<sup>327</sup> OJ L.299/25, 8.11.2008.

<sup>328</sup> Judgment of 12.7.2011 Case C-324/09 (L’Oreal) ECR 2011 I-06011, Para. 64, 131.

<sup>329</sup> Comp. Judgment 10.3.2010 Case C-236/08 (Google France) ECR 2010 I-02417, Para.79.

<sup>330</sup> Judgment of 22.09.2011 Case C-323/09 (Interflora), Para. 36-38, 40.

<sup>331</sup> Judgment of 22.09.2011 Case C-324/09 (Interflora), Para. 4.

distribution. The principle of equal treatment justifies the application of the exhaustion doctrine to both tangible and intangible goods, as well as to services offered on-line.

The DSM, in other words a digital version of the common market, is founded on two principles – free trade and undistorted competition. IP protection interferes or limits both of. IP protection clashes broadly with the protection granted by Articles 101 and 102 of the TFEU. Exemptions justified by TTBER may result in the differentiation of sales on the basis of the territory or customer group. Agreements between non-competing parties may restrict passive sales into an exclusive territory or to an exclusive customer group. The justified TTBER exclusion may, in fact, lead to the monopoly of a rightholder. **The block exemption may not lead to a consumer discrimination on the basis of the territory or customer group.**

However, whilst arguments deriving from IP protection may justify some territorial restrictions, they should not create grounds for discrimination practiced against consumers. The passive sale restrictions implemented in the Internet environment are based on the application of various criteria of consumer categorisation. Depriving consumers from the opportunity to purchase goods or services offered on the digital environment based on the basis of the territory or customer group exclusion is contrary to EU anti-discrimination law, and should not be *de lege ferenda* allowed.

**The Internet has brought about changes to the way of defining goods and services offered digitally.** The general question arising from the unlimited scope of the digital space is whether, or to what extent, legal measures serving to protect the intellectual rights of inventors, researchers, authors should be nationally limited within the EU. IP rules at national level remain territorial, which results to a certain extent in creating specific national market restrictions. The protection of IP rights by specific territorial restraints conflicts with the idea of free movement of goods and services and the idea of harmonised IP. In this context, it should be emphasised that measures, procedures and remedies provided at national level are not allowed to create barriers to legitimate trade<sup>332</sup>.

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<sup>332</sup> Comp. OJ L. 195/16, 2.6.2004. Article 3.

## **6. PROPOSALS FOR EU ACTION**

### **6.1. Proposals related to information and dissemination**

Since both scope and content and in particular any sanctions of the prohibition on discrimination based on grounds of nationality or geographical location may be unknown to businesses, the European institutions could initiate broad information campaigns to this end. As part of such campaigns, a regular monitoring of businesses could be put into place to check whether they offer different conditions of access based on nationality or geographical location. The Parliament could initiate studies which systematically monitor the conditions of access in particular of e-shops. In particular, an official list issued by, for example, the European Commission, naming businesses which provide services throughout the Union with no or hardly any differences, but also naming businesses which differentiate, in particular where there no plausible objective reason is apparent for the different treatment, could be useful in order to increase awareness.

Distinct, but multifarious practices discriminating against the consumer in the DSM are often difficult to identify, due to the specificity of a digital environment and the consumer's lack of knowledge or awareness on existing obstacles. The process of making consumers more aware of the problems of the DSM will make any information initiatives more comprehensive and effective. Consumer information strengthens consumers' awareness of violations, and increases the probability of identifying obstacles. The ability to report discriminatory practices will help in tackling the problems posed by the DSM. Consumers need information and tools to understand and protect their own right not to be discriminated against in the DSM on grounds of nationality or geographical location.

### **6.2. Proposals related to clarification of current regulatory framework**

The analysis highlights the importance of clarification and further unification of current regulatory framework. The clarification of the level and scope of national provisions interfering with EU provision would be recommended in the area of intellectual property.

The principle of fair competition, enshrined in Article 102 of the TFEU, aims to prevent a single company's market power from impairing competitive purchasing, trading and providing services in the DSM. The provision directly protects market competitiveness. Indirectly, however, the provision should protect consumers from the negative effects on monopolistic power. Despite having one of its end-goals as protecting the interests of consumers, the provisions of competition law do not make direct reference to consumers and rules, such as those included in Article 102 of the TFEU are not useful tools for preventing the discrimination of consumers. A consumer-oriented approach is currently lacking and necessary to effectively prevent the abuse of a dominant position on the market and its assessment of Article 102 of the TFEU.

To protect consumers effectively from the many and diverse ways in which businesses take advantage of their weaker economic position requires enacting complex and coherent measures. Provisions setting out the anti-discriminatory rules in the supply of goods and services, consumer protection in a strict sense and consumer rights often overlap with fields covered by EU Competition law. In order to achieve consistent anti-competitive measures the relationship between EU competition law and the law of unfair competition needs rethinking.

Article 20 (2) of Services Directive requires an objective justification for treating persons differently in relation to their nationality or geographical location. However, the scope of the directive is very unclear whereas the main issue is as to whether merely services in the narrow sense of Article 57 of the TFEU (former Article 50 EC) or also sales, in particular



sale of goods, fall within the scope. Moreover, it is unclear whether the protected recipients can only be natural persons, in particular consumers, or also legal persons. Finally, it is questionable whether any enforcement which would create an obligation to enter into contracts would be lawful.

What the European Parliament could do is either initiate a legislative resolution asking the Commission to seek clarification by amending the Directive or, at least, encourage particularly the national courts, possibly also the Commission in infringement proceedings, to bring such issues before the European Court of Justice for clarification.

### **6.3. Proposals relating to improving/revising the regulatory framework**

An analysis of distinct areas of substantive law, including private international law, competition law and intellectual property law, reveals the need for more harmonisation or unification of existing legislation in areas which are likely to have a particular impact on the dynamic of the internal market. To the extent that differences in substantive law form an objective reason for discrimination, the Union could and should remove such differences. Since the harmonisation of consumer protection particularly irons out deep-rooted differences between the member state laws, it could be preferable first to introduce facultative or optional instruments which allow businesses to make use of the internal market under a uniform set of rules.

Improving Article 20 of Services Directive is not an easy task, due to the ambiguity concerning the function of this provision and its placement within the Services Directive. There is a general need to have a provision against discrimination based on residency or establishment. Such a rule should also cover contracts concerning goods and not only services. Rules against discrimination based on non-EU citizenship should also be imposed in such cases. Residency or establishment (in the case of legal persons) should be confined to the territory of the EU. The prohibition of discriminatory practices should not only concern general conditions of access to services used by the service provider, but also cover other contractual practices which infringe this principle – e.g. refusal to contract based on discriminatory criteria. A basic scheme of sanctions must be provided, including compensation and the possibility of demanding that discriminatory practices be put to an end. Such changes would probably require the enactment of a new directive.

The right solution would probably be to repeal Article 20 of Services Directive. The current provisions against discrimination based on nationality of a Member State in Article 18 of the TFEU are sufficient. Residency does not have sufficient support in the Treaties as a self-standing form of discrimination. As far as it concerns discrimination based on residency, Article 20 (2) intervenes too deeply in the decision-making process of the trader and is not fit-for-purpose. Alternatively, the scope of Article 20 (2) of Services Directive could be broadened in order to clarify that contracts on the sale of goods are also covered. The provision could then be turned into a transparency rule which forces certain businesses (e.g. those using distance selling) to clearly indicate any geographical restriction of access to the services and any variations in the terms of their service on grounds of geographical criteria. The Consumer Rights Directive, which is about to be transposed by the Member States, already provides in Article 8 (3) that trading websites shall indicate clearly, legibly and at the latest at the beginning of the ordering process whether any delivery restrictions apply. This is a first step in the right direction.

Particularly on-line shops could be obliged to indicate both geographical delivery restrictions and different conditions based on grounds of geographical location much more prominently. On-line shops should be obliged to indicate that they apply a geographical restriction as well as its justification. Although the EU, as a rule, may not prohibit consumer discrimination in the DSM, EU law may impose a duty of information on businesses which



do so. This would put e-shops under a certain degree of pressure to reconsider their policy and either to explain their restrictive approach clearly or to expand their activity to all member states. An atmosphere of competitiveness towards marketing for the whole EU under the same conditions could be created particularly by studies and communications of the European institutions, which could also inspire the media to report on restrictions applied by prominent service providers. Advertising that “Wherever you are we serve you” could, for example, be used by progressive service providers in order to gain a competitive edge.

Only in market sectors and regions where such measures do not prevent customer discrimination and frustration should the Directive, in a second step, oblige the Member States to apply more invasive measures. The threshold for direct intervention into the market should be rather high. This would be the case were the basic aims of the Union, i.e. the intended constant improvements of the living and working conditions of the citizens and reductions in the differences existing between the various regions, require active intervention to force businesses to offer their services in certain regions. For this case some basic requirements for sanctions should be provided which could include a ban on discriminatory practices and a claim for the compensation of discriminated customers.

First of all, however, EU policy and legislation should improve the conditions for making use of the internal market. Neither competition law, nor intellectual property provisions should condone dividing the market on the basis of a territory or customer group. Forcing businesses by means of the state’s coercive power to be European can only be a second step in situations where the market fails to ensure the equal access of European citizens to the DSM.

Provisions prohibiting discrimination based on geographical location intersects with provisions allowing for restricting in the marketing and sale of products and services on grounds of IP law. Despite the existing level of harmonisation, disparities still exist between different systems of national IP regulation which decreases legal certainty. The development of a unitary European system of IP should be followed by further approximation of IP rights at the national level. To enhance the interplay between IP protection, principles of market freedoms and measures of anti-discrimination on grounds of geographical location, it is highly recommended that efforts to develop uniform protection of intellectual property rights, based on EU-wide measures (e.g. unitary EU patent and further harmonisation and improvement of EU trademark protection) not be abandoned.

#### **6.4. Proposals related to enforcement**

The new European Consumer Agenda<sup>333</sup> emphasised that consumers need tools and information to understand their right to complain and actively influence their rights. Identified practices in the DSM which weaken the economic position of, or even discriminate against, consumers confirm this observation.

Consumers are negatively affected by the lack of measures allowing consumers to report discriminatory practices taking place in the DSM, allowing effective collective redress against undertakings and access to trustworthy ODR schemes. This study highlights the fact that ADR/ODR schemes have an enormous potential to remove barriers to the proper functioning of the internal market.

Taking direct action to enforce *inter alia* Article 20 (2) of Services Directive should be seen as a last resort once other avenues have been exhausted. This may in particular be the

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<sup>333</sup> [http://europa.eu/rapid/press-release\\_IP-12-491\\_en.htm](http://europa.eu/rapid/press-release_IP-12-491_en.htm).

case where the competent authorities detect customer discrimination on grounds of nationality, in particular when this is direct discrimination. Such behaviour would be prohibited under the general rules of anti-discrimination law anyway. It is hardly imaginable that service providers may have an objective justification for directly discriminating against nationals of certain (member) states, be it by denying access or merely by proposing to contract on very harsh terms).

The situation may be very different with regard to discrimination based on the customer's place of residence, although there are many conceivable cases in which hardly any objective reason for, e.g. non-delivery to certain member states could be justified. It may nevertheless be rather drastic to force a business operate in cases where, for instance, the owner merely feels uncomfortable in providing services in certain states, but has no other reason for not doing so. In such a case it should, in the first instance, be left open to the market to determine whether other more adventurous businesses step in and fill the gap. Direct state intervention in order to force unwilling businesses to go abroad should be limited to extreme cases of total market failure and the unbearable exclusion of customers from accessing foreign markets. Increasing state activity is likely to be inefficient and not very likely to ensure that businesses that are forced to serve customers with a foreign place of residence will perform their services to the highest standards.

Enforcement, in particular of Article 20 (2) of Services Directive, would mean forcing businesses to remove from their publicly available conditions of access any restrictive requirement which cannot be objectively justified. In fact, this would mean forcing businesses to conclude contracts with customers, including consumers, with whom they do not wish to conclude contracts. This would, in particular, mean forcing businesses to extend their activities to countries which, for whatever reason, they do not want to target (yet). This would constitute a very invasive form of state intervention into the market and would considerably limit the freedom of businesses. This is probably one of the reasons for the findings of the European Commission that until now hardly any enforcement activity could be monitored in the Union. This is not necessarily bad news since it might be better if EU activities were concentrated upon positively convincing businesses to make better use of the internal market rather than merely forcing them by repressive means.

## 7. CONCLUSIONS

Discrimination against certain types of customer and consumer form an overarching issue. It can arise in many different areas of EU law, be it primary law, private international law and international procedural law, intellectual property law or competition law.

An analysis of consumers' access to goods and services supplied on-line reveals that there is a great deal of discrimination being practiced against consumers in the DSM. Consumers are discriminated by refusal to sell or supply, automatic re-routing without the consumer's consent or knowledge, or the unjustified diversifying of sale conditions. The "Mystery Shopping Evaluation of Cross-Border E-Commerce in the EU" showed that, only in 39 % of cases consumers was possible to place a cross border order without being refused at some point in the process of placing an order. In some Member States there are many products for which consumers cannot find online domestic offers<sup>334</sup>. Consumers active on-line are able to find many popular products offered in cross-border offer at least 10 % cheaper than in domestic on-line purchasers<sup>335</sup>. These findings show that the DSM could potentially be very beneficial for consumers

In the context of discriminatory practices, it is noteworthy that the digital environment is extremely dynamic and that each advance in technology appears to give rise to a new form of discrimination or facilitate traditional forms of discrimination.

Any attempt to resolve such issues at the level of each of the individual areas of law mentioned will necessarily lead to a patchwork regulation, and leave the danger of internal incoherency. It might therefore be preferable to enact overarching legislation in an individual directive which targets the problem for all sectors of the internal market and in particular details the 'side rails' for businesses in order to funnel their use of the internal market without unjustifiably discriminating against customers on grounds of nationality or place of residence.

The freedom to conduct a business and the freedom to provide services in every Member State are fundamental freedoms recognised by the EU. EU primary law protects supports the principle of freedom of contract. Article 18 of the TFEU contains a prohibition on discrimination based on nationality. The criterion of residence could be seen as a case of indirect discrimination based on nationality. The prohibition of discriminatory practices aims to ensure the integrity of the market. Discrimination against consumers in the DSM distorts the European market.

Beside, Article 18 of the TFEU, also Article 20 (2) of Services Directive 2006/123 aims to ensure the proper functioning of the undivided internal market. Although drafted in the terms of EU anti-discrimination law, it should not be regarded as a part of it. It is a rule designed to prevent the internal market from disintegrating. The main reason for problems encountered with the current regulation in Article 20 (2) of Services Directive 2006/123 seems to be that it mixes elements from two rather remote fields of legislation, being, firstly, the anti-discrimination legislation in primary and secondary law as well as case law which usually prohibit certain forms of discrimination (here: nationality and place of residence) and introduce a need for justification in such cases of unequal treatment. Secondly, the provision contains elements from the internal market ideology which is here, in particular, the reference to Article 56 and 57 of the TFEU (former Article 49, 50 EC) and the general conditions of access to services made available to the public at large. These two different backgrounds create nearly insurmountable internal friction between, on the one

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<sup>334</sup> Mystery shopping evaluation (2009), p. 37 f.

<sup>335</sup> Mystery shopping evaluation (2009), p. 39 ff.

hand, the freedom of businesses to decide in which region they wish to be active and, on the other hand, a right of consumers and other customers not to be discriminated against by the refusal to provide services merely on grounds of nationality or place of residence. The result of this mixture is, however, predominantly nothing more than a market-oriented provision directed against a specific market-failure, i.e. the exclusion of European citizens from access to some sectors of the internal market.

Establishing a single competitive market across the EU, which is not territorially divided, is a leading objective of the EU competition law. Practices which impede competition in the traditional common market are as detrimental to the consumer when practices in the e-market. Articles 101 and 102 of the TFEU aim to ensure a competitive market. Competition law limits anti-competitive conduct leading to restrictions on free trade and to market compartmentalisation between Member States. It restricts undertakings from privately creating market barriers and implementing territorial restrictions, which affect the availability of goods or services offered to consumers on the DSM. Anti-competitive constraints and infringements resulting from agreements or decisions of undertakings lead to obstacles which limit consumers' freedom of access to products or services and reduce the competitiveness of retailers active in the DSM, thus creating market barriers. Competition law actually condones various discriminatory practices which otherwise distort competition on the Internet under the block exemptions rules. This means that to some extent competition law allows restrictions of competition which disadvantage consumers. The existing framework limits this anticompetitive exclusion to active sales. There is no general exemption permitting the restriction of passive sales.

Competition law is not a measure of direct consumer protection. It is not applied to B2C relations, and does not aim to protect consumers directly, in contrast to unfair competition provisions. Various practices and agreements which affect consumers in the digital market and cause territorial restrictions are allowed under competition or mergers law. This should not be allowed to diminish consumer protection, nor deprive consumers of the ability to report discriminatory practices infringing their freedoms, implement effective collective redress mechanisms, or directly complain of infringements of their rights. Particular importance must be given to improving the enforcement of consumers' right to redress, since practices impairing competition in the DSM are often difficult to identify and various practices discriminating against the consumer are often not classified as infringing competition, and therefore left out of the remit of competition law provisions.

Anticompetitive effect leading to market compartmentalisation and discriminating against consumers participating in the DSM is brought about by certain aspects of IP protection. IP is not, however, the subject of inviolable and absolute protection. The European exhaustion doctrine provides an effective measure to balance interests of IP rights, competition rules and market freedoms. This doctrine limits IP protection to the level justified by safeguarding specific intellectual property rights. The EU-wide exhaustion doctrine is a measure against long-term market compartmentalisation and limits restrictions of distribution.

The aforementioned measures of primary and secondary EU law provide the framework for the protection of free movement in DSM, which may encourage businesses to sell cross border. There is no easy solution at hand.

In the context of services, the approach of the current legislation, of which Article 20 (2) of Services Directive is the core element, is misguided. Ultimately, it could lead to transforming the fundamental freedom of businesses to make use of the internal market under the Treaty into an obligation to extend their commercial activities to all EU Member States. There is no basis in EU law for doing so.

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## NOTES



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