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RECENT CASES

Reaffirmation of the Prohibition of Agreements Which Restrict Parallel Imports

Re the Agreement of Ford-Werke AG
(82/628/EEC)

The Treaty of Rome (Treaty), establishing the European Economic Community (EEC), sets forth certain practices in article 85(1) which are prohibited as restraints on competition.¹ Article 85(3) tempers the absoluteness of article 85(1) by exempting those practices when the agreements in question have beneficial effects which outweigh any adverse effects on the competitive posture of the parties involved.² Businesses operating in the EEC, therefore, have some degree of flexibility in the types of arrangements into which they enter. In this case, Ford Werke AG (Ford AG) initially distributed vehicles under an agreement which would have been exempt from the proscription in article 85(1). The subsequent change in their agreement, however, brought their conduct within the prohibited activities of article 85(1), and the European Commission (Commission) took action to prevent any further detrimental effect on competition in the EEC. Since the original agreement was acceptable, it remains in force. The Commission struck down the amendment, however, as violative of article 85(1).

Ford AG supplies vehicles to Ford Britain, a Ford subsidiary located in the United Kingdom, and to distributors in Germany.³ The German distributorships function under a Main Dealer Agree-

1. Treaty establishing the European Economic Community, Mar. 25, 1957 II EUR. COMM. TREATIES B (MB) (*in force* Jan. 1, 1958) [hereinafter cited as the Treaty], article 85(1).

2. *Id.* at article 85(3). See also General Note to article 85, *supra* note 1, at B10-197.

3. *Re Agreement of Ford Werke AG*, 25 O.J. EUR. COMM. (No. L. 256) 20 (1982), [1982] 3 Common Mkt. L. R. 267 [hereinafter cited as *Ford Werke AG*]. The decision of the European Commission was appealed to the European Court of Justice. On September 30, 1982, the European Court of Justice upheld the Commission decision. Case No. 229/82. The Court had earlier suspended the Commission's interim order to resume delivery of the right hand drive vehicles on September 6, 1982, but reinstated that order on September 29, 1982.

ment (MDA) which provides for selection of dealers on the basis of quality and quantity. The MDA allocates specific territories for the dealers, who then have a special responsibility for marketing and sales promotion in their respective areas. Dealers are prohibited from selling competing products, from selling to dealers outside the distribution system, and from engaging in certain marketing activities beyond specified areas.⁴ Clause 2(1) of the MDA provides for Ford AG to sell to the main dealers and for the main dealers to sell only to final customers, regardless of their location, and other authorized dealers. It further provides that "[t]he main dealer may sell vehicles to his own downstream organisation and to other main dealers for resale; he may further sell vehicles to dealers resident in another European Community country and authorised to sell such vehicles by a group company"⁵ The MDA defines vehicles as "the standard specification models of all passenger cars, light commercial vehicles and chassis listed in Annex 1 to this Main Dealer Agreement."⁶ The annex lists the commercial names of various models. The ordinary series production vehicles for right hand drive come in two versions. One is sold under Ford AG's Visit Europe Plan and the vehicles are fitted for left hand drive with the speedometer marked in miles. The other version is the German specification model with its speedometer calibrated in kilometers. The prices to the German dealers for these two versions are the same with a processing fee added to the price of those sold under the Visit Europe Plan specifications.⁷ Prior to May 1982, both versions were equally available to German dealers.

As of May 1982, Ford AG stopped making both versions of the right hand drive vehicles available to German dealers. Ford Britain prompted this move because it sold these vehicles at a price higher than that of the German dealers.⁸ Ford Britain lost sales to the German dealers because customers were purchasing cars in Germany and bringing them back to the United Kingdom.

The reason given by Ford AG for terminating sales of the right hand drive vehicles in Germany involved several considerations. First, Ford AG wanted to maintain the higher retail prices existing

4. [1982] 3 Common Mkt. L. R. at 269.

5. *Id.* at 270.

6. *Id.* at 269.

7. *Id.* at 270. Specific figures for prices and quantities sold are not available in the published version of the opinion because of Regulation 17, article 21 regarding nondisclosure of business secrets. *Id.* at note 2.

8. *Id.* at 272.

in the United Kingdom.⁹ Second, since the MDA required the German dealers to exploit as fully as possible their respective marketing areas, by terminating the sale of right hand drive vehicles, German dealers would have to consolidate their sales promotion efforts.¹⁰ Third, because Germany requires only left hand drive vehicles, the right hand drive vehicles are beyond the contemplated sales range.¹¹ Right hand drive vehicles would still be available but only through a Ford subsidiary in London. Ford AG argued to the Commission that "[u]nrestricted parallel imports would bring heavy losses, notably to Ford Britain."¹²

Ford AG's initial agreement with its dealers came within the proscription of article 85(1) which provides:

1. The following shall be prohibited as incompatible with the common market: all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition within the common market.¹³

In this instance all of the necessary elements are present. An undertaking involves a "cooperative effort between two or more entities."¹⁴ The entities can be either individuals or enterprises. Here, there is an undertaking between the German dealers and Ford AG, and there has been an agreement which affects trade between member states.

Regulation 17 of the Council of the EEC provides that an agreement which violates article 85(1) may be notified to the Commission for the purpose of exempting that agreement under article 85(3).¹⁵ Article 85(3) provides:

3. The provisions of paragraph 1 may, however, be declared in-

9. *Id.* at 274.

10. *Id.*

11. *Id.* at 278. Right hand drive vehicles are not, however, illegal in Germany.

12. *Id.* at 274.

13. *Supra* note 1.

14. A. CROTTI, *TRADING UNDER E.E.C. AND U.S. ANTITRUST LAWS* 15 (1977).

15. Council Regulation 17 of February 6, 1962, First Regulation Implementing Articles 85 and 86 of the Treaty, [1959-1962] O.J. 87 (1962) at article 5. No agreement may be considered for exemption under article 85(3) of the Treaty unless it has first been notified to the Commission. The importance of the Commission's role in the notification process cannot be overemphasized. The European Court of Justice cannot unilaterally exempt agreements under article 85(3) of the Treaty. That is within the sole province of the Commission. A. CROTTI, *supra* note 14, at 91.

applicable in the case of:

—any agreement or category of agreements between undertakings . . .

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

- (a) impose on the undertakings concerned restrictions which are not indispensable to the attainment of these objectives;
- (b) afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products in question.¹⁶

Ford AG notified its original MDA to the Commission so as to exempt itself from the provisions of article 85(1). The Commission carried out investigations and decided to initiate proceedings in July 1982, after the original agreement had been modified.¹⁷ It concluded that Ford AG's original MDA would probably have been exempt since similar agreements have been found legal.¹⁸ The modification, however, violated article 85(1) and was not exempt under article 85(3).¹⁹

In this case, the problem arose not because of Ford AG's original agreement, but instead, because of the modification of the original agreement resulting in the termination of the sale of right hand drive vehicles to German dealers. The Commission analyzed the situation which resulted from the May 1982 change in the agreement and decided that the MDA, as modified, came within article 85(1). In coming to this conclusion, the Commission followed its decision in *Re The Application of Bayerische Motoren Werke A.G.*²⁰ In the case at bar, however, Ford AG made a unilateral decision to stop supplying its German dealers with right hand drive vehicles. In *BMW*, the dealers themselves acted so as to pro-

16. *Supra* note 2.

17. *Supra* note 3, at 268.

18. *Re the Application of Bayerische Motoren Werke A.G.*, [1975] O.J. (No. L 29) 1 (1974), [1975] 1 Common Mkt. L. R. D44 [hereinafter cited as *BMW*]. The Commission found that BMW's agreement, although within the terms of article 85(1) of the Treaty, came within the exemption of article 85(3). *Id.* at paragraphs 23-31. Ford AG's original MDA contained many provisions similar to those exempted by the Commission in *BMW*. See *Ford Werke AG*, *supra* note 3, at 276 paras. 28-29.

19. *Supra* note 3, at 281.

20. *BMW*, *supra* note 18.

hibit certain sales.²¹ The Commission, however, did not address this distinction between the two cases. Then, the Commission determined that the agreement did not come within the exemption of article 85(3) for several reasons. First, neither the distribution nor the production of Ford vehicles improved.²² Production of vehicles was apparently unaffected, and distribution was hindered because the agreement prevented German dealers from competing with other dealers as they no longer had right hand drive vehicles to sell. "The practical outcome of Ford AG's unilateral restriction of the term 'vehicle' in the Main Dealer Agreement is that Ford dealers can no longer compete in those areas of the Common Market where vehicles are sold with specifications different from the German ones It leads to the sealing-off of markets within the Community."²³ Second, since the German dealers could no longer be fully operational, the Commission concluded that they could no longer be competitive in their respective marketing territories.²⁴ Third, the Commission ascertained that consumers would be unable to "benefit from price disparities at the retail level."²⁵ Therefore, the public interest would not be served by exempting Ford AG's modified MDA.

The Commission found Ford AG's argument that the modified MDA did not require Ford AG to distribute right hand drive vehicles to German dealers unpersuasive:

It would be incompatible with the very nature of an exemptible distribution system, in which appointed dealers must be able to compete outside their respective agreed areas, if the manufacturer were in a position to specify which vehicles the dealers could sell and in which areas of the Common Market. In fact, under a distribution system, customers must in principle be able to obtain from any appointed dealer all types of the manufacturer's series-production vehicles on sale within the Community. This is particularly pertinent in this case, since Ford AG manufactures right hand drive vehicles itself and sells them in the United Kingdom.²⁶

The Commission determined that trade would be appreciably affected because there were dealers willing to export vehicles but

21. *Id.* at D51-54.

22. *Supra* note 3, at 276-78.

23. *Id.* at 277-78.

24. *Id.* at 278.

25. *Id.* at 278.

26. *Id.* at 279.

who were constrained by the modified MDA. The agreement prevents "cross-border competition in right-hand drive vehicles."²⁷ A detriment to the public interest was found to exist in that consumers were being "deprived of the advantages of a common market."²⁸ For these reasons, the MDA as amended in May 1982, did not come within the exemption of article 85(3). The Commission, therefore, required a return to the situation prior to May 1982.²⁹

The original MDA between Ford AG and its German dealers contained several provisions which by their very terms violated article 85(1) of the Treaty.³⁰ In particular, Clause 5 of the MDA prohibited the dealers from selling competing products.³¹ Regulation 67/67, passed in 1967, would, however, grant an exemption for this particular clause. The dealers were provided with territories in which they had the sole responsibility for marketing and sales promotion but were not prevented from selling to final customers outside of their respective territories.³² These provisions and the EEC's reason for allowing them exemplify the purposes underlying the Treaty.

The Commission recognizes the valid business reasons, not necessarily anti-competitive, for having sole and exclusive distributorships in the context of vertical agreements.³³ The Council of Europe promulgated regulation 19/65 which granted an exemption under article 85(3) to groups of agreements including distributorships in which only two undertakings are parties and one agrees to supply only the other certain goods in a given area.³⁴ The Commission realizes that for many small and medium sized enterprises, the only way to enter a market is by offering a potential distributor some type of exclusive arrangement. Regulation 67/67 "re-affirmed the group exemption for exclusive distributorships . . . and introduced further permissible restrictions on the distributor. For example, it would be permissible to require him not to deal in competitive products."³⁵ The Commission reasoned that:

27. *Id.*

28. *Id.*

29. *Id.* at 281.

30. *Supra* note 3, at 276 paras. 28-29.

31. *Id.* at 269.

32. *Id.* at 270. The distributorships were technically not exclusive distributorships because the manufacturer (Ford AG) was not prevented from selling in those territories. Ford AG, however, did not sell in those areas in this case.

33. A. CROTTI, *supra* note 14, at 134-38.

34. *Id.*

35. *Id.*

[i]n the present status of trade, exclusive distributorship agreements in international trade generally result in an improvement in distribution because an enterprise can concentrate its selling activities . . . and, since it deals with only a single distributor, can more easily overcome the marketing difficulties resulting from linguistic, legal, or other differences. Exclusive distributorship agreements facilitate sales promotion of a product and make possible a more intensive exploitation of the market and a continuous supply while at the same time rationalizing distribution.³⁶

These comments illustrate the pragmatic approach that the Commission has taken in analyzing agreements of undertakings which have been notified to it.

The instant violation arose because Ford AG crossed the fine line separating those agreements which would be exempt under article 85(3)³⁷ and those which would not. Ford AG should have realized that its position was very similar to that of BMW in *Re the Application of Bayerische Motoren Werke A.G.*³⁸ Ford AG's original agreement stayed within the confines of the BMW agreement which the Commission had previously determined to be within article 85(3). Ford AG, however, went one step further and stopped distribution of the right hand drive vehicles to its German dealers. The effect of this action was to prevent parallel exports. The promotion of parallel imports and exports goes to the very essence of the purpose underlying the EEC—to promote the free flow of goods from one member state to another. Although Ford AG did not violate article 85(1), because its decision to stop supplying right hand drive vehicles was unilateral, the Commission did not find this to be an obstacle. It was more concerned with the overall impact on parallel exports in the Community. In addition, Ford AG's primary reason for stopping distribution of the right hand drive vehicles was to maintain the higher retail prices in the United Kingdom. Ford AG went so far as to argue that if it were

36. *Id.* at 136-37.

37. Article 85(3), as it would be applied by reference to regulation 67/67.

38. *BMW*, *supra* note 18. In a subsequent case involving BMW, it modified its original agreement which the Commission had upheld. This time, however, the Commission struck down the modified agreement as violative of article 85(1) and not within the exemption of article 85(3). The modified agreement there was more akin to a horizontal agreement. It restricted trade because the BMW dealers could not compete among themselves, and the result was a restriction of intrabrand competition. 21 O.J. EUR. COMM. (No. L 46) 33 (1978). Ford AG should have realized that its amended agreement would not be tolerated by the Commission since its modification was similar in effect to that made by BMW.

forced to supply the vehicles to the German dealers, it would have to raise the prices to them. This amounted to an attempt to evade the Commission's decision since it would have the same effect as not supplying the vehicles—to discourage parallel exports to the United Kingdom.

Ford AG also argued that by the terms of the modified MDA it was not required to supply right hand drive vehicles. Besides the fact that this argument involved a breach of contract and not the Treaty, the problem with it was twofold. First, the definitions in the MDA of "products" and "vehicles" were so broadly drafted that they could not by their terms exclude right hand drive vehicles.³⁹ The Commission found that "[n]o credence can be given to the assertion that right-hand drive vehicles are fundamentally different from left-hand drive vehicles and that they can no longer be regarded as 'standard specification models' within the meaning of clause 1(2) of the Main Dealer Agreement."⁴⁰ The fact that Ford AG had previously supplied such vehicles to German dealers was particularly devastating to their argument. Second, the Commission determined that if Ford AG's construction of its agreement were accepted, it could not be exempted under article 85(3) since it acted to impede the free flow of goods among member states. The Commission emphasized that consumers must be free to purchase goods anywhere in the EEC from any appointed dealer.⁴¹

Ford AG also argued that, by terminating the sale of right hand drive vehicles to German dealers, it "would make the dealers consolidate their sales promotion efforts in their marketing areas. They would no longer be enticed away from their real contractual function."⁴² In addressing this argument, the Commission noted that Ford AG was unable to "substantiate any neglect of sales in

39. Clause 1(1) of the MDA defined products to include "all vehicles and original parts as defined below and the bodies for vehicles included in the company's supply range. The other goods included in the supply range are the subject of separate agreements, and do not fall within the definition of products for purposes of this agreement." *Supra* note 3, at 269.

Clause 1(2) defined vehicles: "Vehicles means the standard specification models of all passenger cars, light commercial vehicles and chassis listed in Annex 1 to this Main Dealer Agreement." The Annex listed the commercial names of various models such as Fiesta, Escort, and Taunus. *Supra* note 3, at 269. Neither of these definitions are narrow enough to support Ford AG's argument that it was not required by the MDA to supply right hand drive vehicles to the German dealers.

40. *Supra* note 3, at 278.

41. *Id.* at 278-79.

42. *Id.* at 274.

dealers' marketing areas resulting from right-hand drive sales."⁴³ In addition, the MDA contained provisions which Ford AG could utilize in the event dealers failed to fulfill their obligations under the agreement.⁴⁴ Accordingly, the Commission found no merit in Ford AG's argument.

Conclusion

Intrabrand competition involves competition among sellers of the same product. Price differences from one member state to another are very common in the EEC, thereby stimulating intrabrand competition. The Commission has consistently invalidated agreements where the effect of the agreements is to limit or prohibit exports and imports. Such agreements, by attempting to impede the free flow of goods across the borders of member states, infringe upon the primary goals of the EEC. In the instant situation, Ford AG's original agreement undertook to provide that *all vehicles* were available to all of the dealers as long as the vehicles were standard specification models.⁴⁵ Since the original agreement acted to promote free trade, it would have been exempt under article 85(3), in spite of the fact that on its face it violated article 85(1). Once, however, Ford AG acted to limit exports for the express purpose of maintaining higher retail prices in the United Kingdom,⁴⁶ the agreement could no longer be countenanced. It attempted to do exactly that which the Treaty prohibited—impede the free flow of goods between member states.

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43. *Id.*

44. Clause 6 of the MDA provided Ford AG with the necessary procedures. *Id.* at 281.

45. *Id.* at 277.

46. Even without the express purpose of maintaining higher retail prices, the agreement, as modified, would have been struck down since its effect was to limit parallel exports.