

PUBLIC CONSULTATION
ON REVIEW OF COMPETITION RULES FOR DISTRIBUTION

COMMENTS OF HERMÈS
ON THE REVISED VERTICAL RESTRAINTS BLOCK EXEMPTION AND GUIDELINES

Introductory remarks

Hermès International Sca., holding of the Hermès Group (hereinafter “Hermès”), welcomes the opportunity to respond to the request of the European Commission (“Commission”) for comments on its proposal for a revised block exemption regulation on vertical agreements and Guidelines on vertical restraints, published on 28th July 2009.

Founded in 1837, originally craftsman of renowned harness for horses, Hermès nowadays designs, develops and markets exceptional products including leather goods, menswear and women's fashion, watches, lifestyle accessories and perfumery products. Hermès products result from a combination of high-quality materials and appraised hand-craftsmanship, implementing the traditional techniques into original creations. Such characteristics make Hermès products rare and singular.

The attention devoted to the development of Hermès products has always been followed by a sale ritual where the product is inserted in a particular universe, where aesthetics is combined with functionality, where each product carries a name, tells a story; which is also transmitted by the salesperson.

And such ritual is not depleted when the client leaves the boutique: when a client buys a Hermès product, he can be confident that he will benefit from an after-sales service through which he can exchange or have his article repaired in any Hermès boutique around the world.

During the second half of the 20th century, Hermès has set a distribution model coherent with the singularity of its products and clients, in compliance with the distribution law in force; through its fully-owned stores, through stores operated by its third party partners or through approved retailers.

The development of the virtual world has presented challenges for Hermès regarding its distribution model, but Hermès has endeavored to use the internet as a complement of its brick-and-mortar distribution network and that for the products which are compatible with such distribution (in terms of production capacity).

Hermès has put in place an internet site which, at the same time, enables internet sales and is a channel for its clients to be in touch with Hermès values and ideas, cultural activities and patronage of the Fondation Hermès and to interact with Hermès by using its website as a screen for the client’s personal Hermès’ experiences.

Indeed, Hermès has been one of the pioneers of the development of internet sales through its site hermes.com, launched in the United States in 2002 and in France in 2005.

The development of the internet site hermes.com has been followed by the development of a “Hermès Web Corner” made available to Hermès approved retailers.

Hermès, as a member of the *Comité Colbert*, agrees with all of the comments made by the *Comité Colbert* on the draft vertical restraints block exemption and guidelines. However, in addition to the observations made by the *Comité Colbert*, Hermès would like to stress the following points in relation to selective and online distribution.

I. The current draft of Article 4(b) undermines the concept of selective distribution

Article 4 of the Commission’s draft block exemption regulation identifies a number of hardcore restrictions.

Territorial bans on sales are listed as hardcore restrictions, one of the exceptions being “the restriction of sales by the members of a selective distribution system to unauthorised distributors in markets where such a system is operated” (Article 4(b) third indent, emphasis added).

If Hermès understands this phrase correctly, the Commission’s objective is to prevent suppliers from restricting sales to unauthorised distributors in territories where the supplier sells its products to non-selective distributors.

However, Article 4(b), third indent, of the draft block exemption regulation could be misinterpreted to mean that in a territory where a selective distribution system is not in place for a certain product, a supplier may no longer prevent an authorised retailer from selling to an unauthorised retailer in that territory.

In addition, where a supplier has exclusively reserved given territories for its own direct sales to final customers, Article 4(b), third indent, could be misunderstood as allowing an authorised dealer to sell to an unauthorised dealer in a territory exclusively reserved to the supplier itself.

Such interpretations are contradictory to the concept of selective distribution which allows a supplier to prevent its authorised retailers from selling to unauthorised retailers, wherever the latter may be located. In such circumstances, the selective distribution networks of goods which are not distributed throughout the whole of the EU would no longer be secure and could be undermined.

Therefore, Hermès asks the Commission to revert to the wording of Regulation 2790/1999 and remove the words “in markets where such a system is operated” from Article 4(b), third indent.

II. The market share of the distributor unduly limits the scope of the exemption

The new Article 3 of the revised block exemption regulation provides that the exemption shall apply on condition that the market share held by each undertaking party to the agreement does not exceed 30% on any relevant markets affected by the agreement.

Hermès is of the view that the introduction in Article 3 of distributor market share reduces legal certainty and limits the scope of the block exemption regulation applicable to distribution networks.

Indeed, with regard to selective distribution networks, this change will be extremely difficult to implement since the market shares on catchment areas will be very difficult to estimate and to monitor, given the absence of statistics about the vast majority of the markets potentially concerned and might also differ significantly from one cluster to the other. By creating such uncertainty, the proposed new Article 3 actually jeopardizes the benefit of the block exemption, to the detriment of both the supplier and the distributors.

The revised Article 3 is, in any case, not necessary in light of the possibility given by Article 6 to the competition authorities to withdraw the benefit of the regulation where it is found in any particular case that vertical agreements to which the regulation applies nevertheless have effects which are incompatible with the conditions laid down in Article 81(3) of the Treaty.

III. The legitimacy of selective distribution for Hermès luxury goods

The EU Courts and the Commission have long recognized that certain industries, in particular for luxury goods, may legitimately organize their distribution model in particular in the form of selective networks within which distributors are selected based on specific criteria and agree on specific high-quality requirements.

The development of internet does not call into question this basic principle so long as the same atmosphere is recreated in the e-boutique virtual environment.

Suppliers of rare and singular products like Hermès should be allowed to require from their retailers compliance with this requirement to ensure that the online buying experience is a seamless extension of the buying experience in the boutiques.

As indicated in the introduction to this document, the Hermès boutiques play a prominent role in the buying experience of products and are one of the key elements of Hermès creativity and tradition.

Paragraph 54 of the new draft Guidelines, which makes it clear that “...under the block exemption the supplier may require its distributors to have a brick and mortar shop or showroom before engaging in online distribution”, is in line with this requirement.

For the same reason, Hermès welcomes the principle set out in paragraph 57 of the new draft Guidelines whereby the criteria for on-line sales by authorised retailers must pursue the same objective as those required for off-line sales.

In addition, Hermès would like to emphasize that in its case, online sales are constrained by the scarcity of the some of its products.

Some of Hermès products require a significant number of hours of hand-craftsmanship based on long-standing and traditional techniques. These hours spent by talented master craftsman cannot be replicated to meet the purported requirement that products should be available to everyone without restrictions through e-commerce.

For all these reasons, some particular houses must remain free to organize their business models as they see fit, in particular, through selective distribution networks. The scarcity of some of Hermès products reinforces the legitimacy of such selective distribution including the control of online sales.

IV. The legitimacy of selective distribution should not be undermined by internet

Admitting that competing distributors could free ride and benefit from an effort without having to commit to the same expenses may put some companies in a unfavorable position, with less incentives to creativity development and network investments; not only regarding fixed assets, but also important investments in terms of sales forces and promotion expenses (exclusive and prestigious locations, stocking extensive product ranges, attractive displays, merchandising, trained staff, customer services, etc.).

In other words, internet creates free riding opportunities for certain players to unduly benefit from the investments made by manufacturers and their authorised retailers in their selective networks. The unregulated expansion of the internet would weaken the viability of the physical network to the detriment of the consumer, jeopardizing the luxury aura of the brands. In addition, unregulated internet selling facilitates the growth of counterfeiting, putting consumers at risk.

These threats potentially jeopardize the economic incentives of traditional houses like Hermès to continue investing in quality, creation and innovation. They reinforce the legitimacy of selective distribution systems adopted for the sale of luxury goods, and reinforce the need for coherence on online sales.

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Hermès appreciates the opportunity to submit these comments and hope that they are helpful to the Commission as it finalizes its revised block exemption regulation and Guidelines.