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Prohibition on Sales at a Loss | A Foregone Conclusion

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The regulation concerning retail trade contravenes European law as regards sales at a loss

On 19 October, the European Union Court of Justice issued an interesting judgment as part of a preliminary ruling proceeding on the possible incompatibility of article 14 of Law 7/1996 concerning Retail Commerce (RCL) −that establishes a ban on sales at a loss− with Directive 2005/29/CE, of 11 May, on unfair business practices (the "Directive"), whose transposition was effected by virtue of Law 29/2009 of 20 December[1].

Main claim

The preliminary-ruling issue was raised by Contentious-Administrative Court 4 of Murcia in the context of a challenging action filed by a wholesale company against the €3,001 sanction imposed by the Directorate-General for Trade and Consumer Protection for a case of sale at a loss.

The Court of Justice's rationale

The Court of Justice's rationale —in line with the criterion exposed by the General Attorney in his conclusions filed on 29 June, which confirms the position already maintained when Belgium's regulation regarding prohibition on sales at a loss was analysed[2]— can be summarised as follows:

[1] Law 29/2009, of 30 December, amending the legal system governing unfair competition and advertising to provide more protection for consumers and users, that amended, among others, RCL (article 18) and the Unfair Competition Law (articles 4, 5 and 7).

[2] See court order of 7 March 2013, Euronics Belgium, C-343/12.

1) The aim of RCL and, specifically, of article 14 on the prohibition of sales at a loss, is (among others) the protection of consumers (RCL's own recitals so recognise). If this is the case, RCL falls within the scope of application of the Directive[3].

2) Sales at a loss are not included on the list of 31 unfair business practices expressly prohibited, without the need of a detailed analysis, as stated in Annex I of the Directive. This is a comprehensive list, that cannot be extended by the Member States. Therefore, the ban on sales at a loss can only be declared unfair on a case-by-case basis, depending on whether it is unfair according to the criteria laid down in the Directive itself (articles 5 to 9, that is, when it is aggressive and misleading)[4].

3) However, article 15 RCL involves a general prohibition on sales at a loss. The fact that the regulation includes two exceptions (when direct competitors' prices are reached, or in case of *in-extremis* sales of perishable goods), does not prevent the prohibition from being considered the general rule. Furthermore, these exceptions arise from criteria that are different from those established in the Directive, and involve an undue reverse of the burden of proof, as companies are the ones that have to prove the existence of any of these exceptions.

4) Therefore, the general prohibition included in article 14 RCL contravenes the Directive, that fully harmonises regulations concerning unfair business-to-consumer commercial practices, so that States cannot adopt measures that are more stringent than those included in the Directive, not even to ensure further protection[5].

Consequences for the FMCG world

Legal implications

According to the Court of Justice, article 14 RCL contravenes the Directive. Pursuant to the principle of primacy, not only does this compel the State to amend RCL (for example, adapting the prohibition to the Directive's criteria), but it allows companies to invoke this incompatibility vis-à-vis the Administration, since it seems clear that, in this case, the three requirements established by Community case-law to recognise the direct vertical effect of directives have been met:

[3] As stated Recital 6, the Directive intends to approximate the laws of Member States on unfair commercial practices which directly harm consumers (regardless of whether, indirectly, they may also be harmful for competitors).

[4] In which the three cases indicated in article 17 of Law 3/1991 on Unfair Competition (UCL) fit: when the practice misleads consumers as regards the level of prices of other products or services in the same establishment; when the practice is derogatory as it undermines the image of somebody else's product or establishment; or when the practice is predatory because it is part of a strategy aimed at eliminating a competitor or group of competitors from the market.

[5] See point 29 of the judgment and article 1 of the Directive that bases this principle on the need to guarantee the functioning of the internal market.

- the transposition term has expired;
- the adaptation of the relevant Directive by the Member State has been carried out inefficiently or not carried out at all[6];
- the invoked provision is precise and unconditional enough as to allow its direct effect.

Strategic implications

Going forward, as regards the distribution and consumer-goods sector, not just the food sector, the impact of the Court of Justice's judgment may be relevant from a strategic standpoint, to the extent that it can affect the negotiations among the different operators throughout the whole chain:

1) It is commonly said that the measures against sales at a loss have been adopted in some countries –among others, Spain– to restrict retail distributors' freedom to set very low prices to attract clients.
2) From now on, the Administration should refrain from applying article 14 RCL and should not open files or impose sanctions for sales at a loss.

"The judgment may affect negotiations between manufacturers and suppliers of consumer goods and distributors, triggering a price war in the retail sector, especially for branded products".

3) Once the restriction is removed, sales at a loss carried out by retail distributors can only be prosecuted within the provisions laid down in article 17 RCL.
4) Yet, it seems unlikely that this path could have any relevant outcome. Indeed, invoking RCL would require, on the one hand, proving the existence of any of the scenarios described in article 17.2 (that is, that the practices have misleading effects for consumers, derogatory effects for the products, or predatory ones for retailers' competitors); and, on the other hand, filing proceedings before commercial courts, with all that such an action would entail in terms of time and money, as opposed to the implications of a report to consumer authorities.
5) Therefore, from now on, distributors that wish to do so can be expected to contemplate the establishment of a low-price policy, even below acquisition prices.
6) In our opinion, this situation may generally affect negotiations between manufacturers and suppliers (especially of branded products) and major distributors.

[6] It should be noted that the judgment of the European Union Court of Justice considers article 14 should be considered a transposition –a wrong one in any case- of the Directive as, like the Attorney General says: *"(…) the option to retain national provisions constitutes an act of transposition of a Directive as legitimate as making substantial changes, such as the re-drafting or deletion national Law provisions".*

7) Up to now, all of them had a reference to rely on —the selling price stated in invoices, which is usually the same for all the distributors— from which distribution prices could not be lowered. This situation has eased annual price-review negotiations, as distributors could have some kind of assurance —and manufacturers could provide it— that they would not lose competitivity vis-á-vis other distributors: if prices set by suppliers on invoices are the same for all, and they cannot sell below such prices, it is easier for distributors to accept the annual price increases proposed, provided that suppliers and distributors share the profits resulting from price increases through the partial assignment of such increases by means of off-invoice discounts that, according to article 14.2 and 14.3 RCL, are not taken into account when the prohibition established in article 14.1 is applied.

8) As a result of article 14 RCL having been declared to contravene Community regulations, this reference disappears and this might well result in a price war in the retail sector, which would most likely and immediately result in an upward-pressure for suppliers.

9) Lastly, it can be assumed that this situation —if it takes place— will mainly affect manufacturer-branded products, not so much private labels, which should ultimately contribute to reduce the price gap existing between both categories.

The impact of the regulation that prohibits sales at a loss has been studied in other European legal systems such as the French and Irish, concluding that, in general, its existence has inflationary effects.

As regards the role that sales at a loss play in fostering balance in the negotiation between manufacturers and distributors, reference should be made to Decision 14-D-19 issued by the French competition authority, whereby several manufacturers of consumer-good products are sanctioned for collusive arrangements after the reform of the Galland Law in France.

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For any further comments or queries on the content of this document, you may contact:

- Diego Crespo (Competition & Distribution Law)

  dcrespo@marimon-abogados.com

- Nathalie Klefisch (Public & Consumer Law)

  klefisch@marimon-abogados.com