



GUIDELINES ON VERTICAL AGREEMENTS

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INTRODUCTION

(1) Article 5 of the Act no 4054 on the Protection of Competition vests the Competition Board (the Board) with the power to issue communiqués which grant block exemptions to types of agreements fulfilling certain conditions, as well as to determine the conditions in question. Vertical agreements, which enable undertakings to establish the production and distribution process in the best possible way and which, as a result, ensure an increase in inter-brand competition in the market, are among the main groups of agreements which should be exempt from the prohibition of article 4 of the Act. As a matter of fact, with the Block Exemption Communiqué on Exclusive Distribution Agreements no 1997/3, Block Exemption Communiqué on Exclusive Purchasing Agreements no 1997/4, Block Exemption Communiqué on Franchise Agreements no 1998/7 and Block Exemption Communiqué on Motor Vehicles Distribution and Service Agreements no 1998/3¹, the Board has granted block exemption from the application of article 4 of the Act to those vertical agreements fulfilling the conditions set forth in the relevant communiqués. Even though the block exemption communiqués listed above are quite detailed, as a result of recent experiences, it has been determined that they cover only a limited portion of vertical agreements. The Board has issued the Block Exemption Communiqué on Vertical Agreements no 2002/2, which replaced three of the above-mentioned block exemptions with the exception of Communiqué no 2005/4, and which, more importantly, is significantly larger in scope. The Communiqué in question was amended by the Communiqué no 2007/2, which was published in the Official Gazette on 25.5.2007. The most important effect of the said amendment was the restriction of the scope of the Communiqué with the introduction of a 40% market share threshold. The purpose of these guidelines is to clarify, to the extent possible, the points that will be taken into consideration by the Board both in the application of the Communiqué, and in the assessments to be made within the framework of article 5 of the Act concerning those vertical agreements which are not covered by the Communiqué, so as to minimize any uncertainties that may arise in the interpretation of the Communiqué as well as of article 5 of the Act as regards vertical agreements concluded by undertakings.

(2) Undertakings wishing to request individual exemption for those vertical agreements which are not covered by the Communiqué may notify the Board in accordance with the Guidelines on the Voluntary Notification of Agreements, Concerted Practices and Decisions of Associations of Undertakings.

¹ Communiqué no 1998/3 was abolished with the entry into force of the Block Exemption Communiqué on Vertical Agreements and Concerted Practices in Motor Vehicles Sector no 2005/4 (Communiqué no 2005/4) on January 1, 2006.

1. THE SCOPE OF THE BLOCK EXEMPTION

1.1. The Definition of "Block Exemption"

(3) Article 2 of the Communiqué, titled "Scope," defines vertical agreements as "Agreements concluded between two or more undertakings operating at different levels of the production or distribution chain, with the aim of purchase, sale or resale of particular goods or services." As stated in article 7 of the Communiqué, this Communiqué is applicable to vertical concerted practices in addition to vertical agreements under the same criteria. Based on the definition of "vertical agreement" included above, three important points must be emphasized:

- There must be two or more undertakings parties to the agreement. Therefore, agreements concluded with end users lacking the characteristics of an undertaking are not subject to block exemption since they are not covered by article 4 of the Act. However, it should be noted that such commercial transactions concluded between undertakings and end users lacking the characteristics of an undertaking may still fall under the scope of article 6 of the Act.
- Undertakings parties to the agreement must be operating at different levels of production or distribution. A distribution agreement signed between a producer in the position of a supplier and a wholesaler is, therefore, a simple example for vertical agreements. A supply agreement signed between an undertaking in the position of a raw material producer and another undertaking which uses that raw material in production also falls within the definition of vertical agreements specified by the Communiqué. An agreement signed between a firm in the position of a producer, a distributor in the position of a wholesaler and, finally, a retailer which sells the products to consumers is also seen as a vertical agreement and may benefit from block exemption, provided it fulfills the conditions set forth in the Communiqué. The important point here is that undertakings parties to the agreement must be operating at different levels of distribution. Otherwise, for instance where an undertaking in the position of a wholesaler concludes the same agreement simultaneously with more than one supplier firm operating one level above in the distribution process, the vertical agreement definition provided by the Communiqué is not applicable to the relevant agreement. Instead of concluding the same agreement with competing suppliers simultaneously, the wholesaler undertaking must sign the relevant agreement with each of the suppliers separately.
- The agreement must aim the purchase, sale or resale of particular goods or services. Accordingly, the Communiqué covers both purchase (supply) agreements and distribution agreements. In other words, the purpose of the buyer when purchasing the goods and services in question is not important. The buyer may have bought the relevant goods or services for the purposes of resale or for use in its own production. Moreover, even if the buyer has purchased the relevant goods from the supplier in order to lease them to third parties, the agreement signed with the supplier will fall under the definition of vertical agreements established in the Communiqué. However, leasing contracts signed between the buyer and third parties (for instance financial leasing contracts) are not considered vertical agreements, since they do not concern the purchase, sale or resale of goods or services in any way.

1.2. Vertical Agreements Which Include the Exercise of Intellectual Rights

(4) In case a vertical agreement which includes arrangements concerning the purchase, sale and resale of goods and services also contains provisions on the transfer of intellectual rights to the buyer or the exercise of such rights by the buyer, the relevant vertical agreement may benefit from block exemption, provided that certain conditions are fulfilled. Article 2.4 of the Communiqué, titled "Scope," specifies the conditions that must be fulfilled in order for vertical agreements including the transfer of intellectual rights to the buyer or the exercise of such rights by the buyer to benefit from the block exemption. Such vertical agreements may be assessed under the block exemption, provided all of the conditions explained below are met:

- Provisions concerning intellectual rights must be directly related to the use, sale or resale of the relevant goods and services.

- The purchase, sale or resale of the goods and services concerned must be the main purpose of the agreement. In other words, the transfer of intellectual rights to the buyer or the use of such rights by the buyer must serve the purchase, sale or resale of the goods and services concerned, and should not comprise the main purpose of the agreement. This condition is generally fulfilled in franchise agreements. In order to maintain the uniformity of the franchise system, intellectual rights transferred to the franchisee are, in general, supporting factors required for the purchase, sale or resale of the goods and services concerned. However, the Communiqué may not be applied to, for instance, plain license transfer agreements, since such agreements do not concern the purchase or sale of goods or services in any form.

- A point of note is who transfers the rights to whom with the agreement. In case there is a transfer of intellectual rights to the buyer or a use of such rights by the buyer, the agreement may benefit from the block exemption granted by the Communiqué. Otherwise, in case the rights are transferred from the buyer to the supplier and some limitations are introduced on the sales of the supplier, such a vertical agreement may not benefit from the block exemption. For instance, in contract manufacturing agreements, the undertaking in the position of the manufacturer and supplier (contractor) generally acquires the know-how necessary for production from the undertaking in the position of the buyer. The practice of chain markets establishing their own brand by having a manufacturer produce private-label brands may be assessed under the framework of the Communiqué, if the chain market does not manufacture the goods in question and does not transfer any know-how on the subject to the manufacturer.

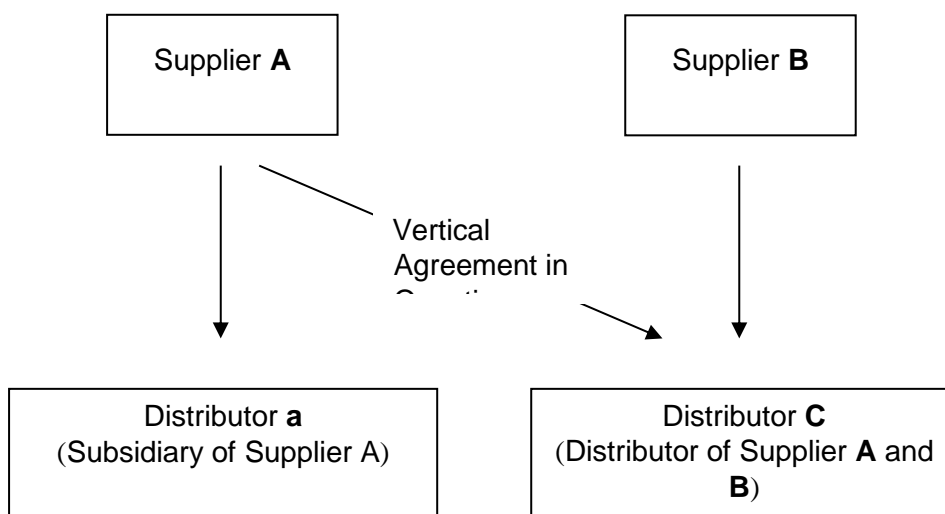
- Provisions concerning the transfer and exercise of intellectual rights must not include restrictions on competition which have the same purpose or effect with those vertical restrictions which are not exempted by the Communiqué.

1.3. Vertical Agreements between Competing Undertakings

(5) In accordance with article 2.5 of the Communiqué, vertical agreements between competing undertakings may not benefit from block exemption, barring exceptional circumstances. The term "competing undertakings" is defined under article 3.1(c) of the Communiqué. Accordingly, suppliers which operate or have the potential to operate in the same product market in Turkey are considered competing undertakings,

regardless of whether they are in operation in the same geographic markets. Those undertakings which are not currently producing competing goods but which can make the necessary investments and enter the market within one year in case of a relatively small but permanent increase in the prices of the relevant goods will be evaluated as undertakings with the potential to operate in the product market in question. When determining the potential for any undertaking to make such an investment and enter into a new market, a realistic approach based on the available data will be used instead of a theoretical one. For instance, an undertaking will not be considered a potential competitor in a market that is completely separate from the market in which it currently operates, regardless of how much financial power it may hold. However, if it is clearly known that this undertakings is planning to enter into the market in question, it will then be considered a potential competitor for that market.

(6) An exception was introduced for the provision that vertical agreements between competing undertakings may not benefit from block exemption, which provides that undertakings may be competitors but only at the distribution level. In other words, vertical agreements where the supplier is both the manufacturer and the distributor of the goods concerned while the buyer is not the producer of competing goods but the distributor may benefit from the block exemption. Thus, undertakings in the position of a producer can distribute their products through independent buyers while at the same time engaging in the distribution of their goods themselves. The exception in question is shown in the figure below with the help of an example:



(7) As seen in the figure above, Supplier A and Supplier B are two competing undertakings operating in the same product market. Supplier A sells its products both through its subsidiary (Distributor a) and through the vertical agreement signed with the independent Distributor C. Due to the fact that Distributor C also distributes the products of Supplier B and that Supplier A is also active in the distribution level via Distributor a, Supplier A and Distributor C are competitors at the distribution level. Since these two undertakings are not competitors at the production level, the vertical agreement concluded between them falls within the scope of the Communiqué. However, if Distributor C were a subsidiary of Supplier B, Supplier B would be

distributing the products of its competitor, Supplier A, and the agreement in question would not benefit from the block exemption granted by the Communiqué.

1.4. Relationship with Other Block Exemption Communiqués

(8) Article 2.6 of the Communiqué states that this Communiqué shall not be applicable to vertical agreements that fall within the scope of another block exemption communiqué. Thus, in case communiqués concerning a certain subject or sector exists, these communiqués which include more detailed and specific regulations will be applied instead of the more general Communiqué no 2002/2. For instance, it is not possible to evaluate a vertical agreement concerning the distribution of motor vehicles under the scope of the Communiqué no 2002/2. Such an agreement may only be assessed under the Communiqué no 2005/4.

1.5. Agency Agreements

(9) Undertakings may sometimes prefer to use the agency system in the purchase and sale of goods and services, instead of using independent undertakings. The Turkish Code of Commerce defines an agency as "a person whose profession is to permanently mediate agreements concerning a business or to conclude such agreements on behalf of that business within a specific location or region, on the basis of a contract and without a subordinate title such as commercial representative, commercial proxy, sales officer or clerk." For instance, the relationship between an undertaking which sells plane tickets and the airline is, in general, an agency relationship.

(10) Since the limitations placed on the agency concerning the agreements it mediates or concludes on behalf of its client are not generally under the scope of Article 4 of the Act, they are, in principle, not a subject of the exemption regime. The fact that the agreement signed is called an agency agreement does not, by itself, mean that the agreement in question is not covered by Article 4 of the Act. In this situation, the factor which determines whether or not the relationship between the undertakings falls under article 4 of the Act is whether the agency takes a commercial or financial risk in relation to the activities assigned to it by its client. In case the agency does not assume any financial or commercial risks due to the agreement it concludes or mediates, then the relationship between the agency and its client is beyond the scope of article 4 of the Act. In such a case, the buying or selling activities of the agency is considered part of its client's activities. The client undertaking, as a result of the agency service it receives, will gain the right to determine the economic activities of the agency in this area, in exchange for taking the financial and commercial risks. In the opposite situation, the agency undertakes all of those risks itself and therefore would need to freely set its own marketing strategy in order to ensure a return of its investments. Under those circumstances, the agreement in question may fall under article 4 of the Act and may be assessed under the Communiqué.

(11) All undertakings engaged in commercial activities are under a certain amount of risk, even if limited. For instance, the profits of an agency are based on its own performance. Similarly, an agency which invests in the facilities out of which it operates and in its staff is also under risk. However, the fact that the agency undertakes such risks related to the maintenance of its activities as an agency does not mean that the relationship between the parties fall within the scope of article 4 of the Act.

(12) When evaluating the risk, which is a determining factor in the application of article 4 of the Act, specific conditions of each case will be considered on their own. In other words, when determining which party undertakes the risk, the assessment of the legal relationship between the parties will not be deemed sufficient, and the economic conditions of the market will also be taken into account. In case one or more situations listed as examples below, the relationship between the parties will be addressed under the scope of article 4 of the Act:

- Contribution by the agency in the costs related to the purchase and sale of the goods or services, including transportation costs.
- Forcing the agency to contribute, directly or indirectly, to activities aimed at increasing sales.
- The agency assuming risks such as the funding of the contracted goods kept at storage or the cost of lost goods, and the agency being unable to return unsold goods to the client.
- Placing an obligation on the agency for provision of after-sales service, maintenance or warranty services.
- Forcing the agency to make investments which may be necessary for operation in the relevant market and which can be used exclusively in that market.
- Holding the agency responsible to third parties for any damages caused by the products sold.
- The agency assuming responsibility other than failing to get a commission due to customers' failure to fulfill the terms of the contract.

(13) The agency must not undertake the risks and costs listed above in order to ensure that article 4 of the Act is not applicable to the relationship between the client and the agency. Risks and costs mentioned here are given as examples and it is possible to add other items to the list.

(14) Agency contracts generally also include provisions which regulate the relationship between the agency and the client. These agreements can include restrictions which prevent the client from appointing another agency for the relevant transactions at the customer or regional level (exclusive agency clause) and/or prevent the agency from serving as an agency or distributor for competing undertakings (non-competition clause). Exclusive agency clause only concerns intra-brand competition and does not generally lead to anti-competitive effects. However non-competition obligations, including those related to the period following the termination of the agreement, concern inter-brand competition and may lead to anti-competitive effects if they create a foreclosure effect in the relevant market where the contracted goods and services are being sold; as a result, this provision may fall under article 4 of the Act.

(15) Even when the aforementioned or similar financial and commercial risks are undertaken by the client, the agency agreement may still fall under the scope of article 4 of the Act, if it facilitates anti-competitive cooperation. This situation may arise

particularly when several clients use the same agency and transfer important information to each other through the agency.

2. RESTRICTIONS WHICH EXCLUDE AGREEMENTS FROM THE SCOPE OF THE BLOCK EXEMPTION

(16) Vertical agreements which include any of the restrictions listed in article 4 of the Communiqué may not benefit from the block exemption and consequently fall under the scope of the prohibition of article 4 of the Act.

2.1. Resale Price Maintenance

(17) Article 4.1(a) of the Communiqué concerns obstruction of the buyer undertaking's freedom to determine its own prices. Accordingly, setting fixed or minimum sales prices for the buyer is absolutely prohibited. However, the supplier may set maximum sales prices for the buyer or offer recommended sales prices to the buyer, provided these do not transform into fixed or minimum sales prices. In order to ensure that maximum or recommended sales prices notified to the buyer do not become minimum or fixed prices, price lists or packaging of the product must clearly indicate that the prices concerned are maximum or recommended prices.

(18) Besides directly maintaining the buyer's sales prices through the inclusion of explicit provisions in the vertical agreements signed, supplier undertakings can also commit the same violation indirectly through various practices. Setting the profit margin of the buyer, setting the maximum rate of discount that may be implemented by the buyer over a recommended price level, providing discounts to the buyer to the extent that the buyer complies with recommended prices or threatening the buyer with delaying and suspending deliveries or terminating the agreement in case the buyer does not comply with those recommended prices or the actual implementation of such penalties may be given as examples of indirect resale price maintenance. Such indirect practices of resale price maintenance fall under article 4.1(a) of the Communiqué as well.

(19) Direct or indirect methods of resale price maintenance will be more effective where the prices implemented by the buyer can be monitored and controlled by the supplier. For instance, an obligation introduced on all buyers to report those buyers who sell at prices different from those included in the standard price lists would significantly facilitate the control of the supplier over the prices implemented in the market. Similarly, most favored customer clauses included in agreements between undertakings may reinforce the impact of direct or indirect methods for resale price maintenance, since they may decrease the supplier's incentives to sell the products to buyers other than the favored customer for better prices and conditions. However, the most favored customer clause and similar supporting practices which reinforce the effectiveness of resale price maintenance should not be seen as practices that lead to resale price maintenance on their own.

2.2. Region and Customer Restrictions

(20) Article 4.1(b) of the Communiqué concerns the restrictions placed upon buyers concerning the region or customers the contracted goods or services may be sold. Accordingly, barring the four exceptions listed in the article, the buyer may not be

placed under region or customer restrictions. At this point, an explanation should be given on how region and customer allocation may occur in practice. It would not be hard to detect a violation if there are provisions in the contract which prevent sales to certain groups of customers or to customers in certain regions. However region or customer allocation may also occur through indirect means. Supplier undertakings can take deterrent measures in order to ensure that demands from a certain region or customer group are not fulfilled, even when the contract contains no prohibitions in any form. For instance, reducing or eliminating the awards or discounts provided to buyers who make sales to customers other than those determined by the supplier, reducing the amount of the goods supplied, or a complete refusal to supply are among the types of conduct most frequently encountered in practice concerning region and customer allocation. In case there is a practice in the market such as giving serial numbers or labels to the goods indicating which buyer released the goods to the market, practices aimed at customer and region allocation may become even more effective. Provided that there exists an objective reason related to the product, a ban on all buyers not to sell to certain customers will not be deemed a restriction excluding the distribution agreement under examination from the scope of the block exemption. For instance, undertakings in the position of suppliers for certain dangerous materials may prevent the buyers from selling such goods to certain customers based on safety or health concerns.

(21) The types of region or customer allocation listed under four headings in article 4.1(b) of the Communiqué are not seen as restrictions which exclude agreements from the scope of the block exemption. The first of these exceptions allows, in particular, supplier undertakings wishing to establish a distribution network to grant exclusive sales regions or exclusive customer groups to themselves or to buying undertakings. For example, a producing undertaking in the position of a supplier can distribute its products through the distributors it assigns to each province in Turkey and can provide regional protection for the distributors. Similarly, a drug manufacturer, for instance, can create exclusive customer groups by ensuring that distribution firms which distribute their products to pharmacies and to pharmaceutical warehouses participating in tenders² are separate. Supplier undertakings may also allocate customers among the buyers both in terms of regions and in terms of customer types simultaneously. An undertaking producing pharmaceuticals assigning different distributors to hospitals and pharmacies in each province can be given as an example to the simultaneous use of region and customer allocation.

(22) The protection provided to undertakings via the grant of an exclusive region or customer group is not absolute. When selling to the region or customer group assigned to them, buyer undertakings can only be protected from active competition by the other buyers in the system. In other words, the supplier undertaking may restrict active sales to exclusive regions or customer groups assigned to itself or to a buyer. Restriction of passive sales to that region or customer group shall be considered an infringement which excludes the agreement from the block exemption. At this point, the distinction between active sales and passive sales becomes important.

(23) Sales to individual customers in the exclusive region or exclusive customer group of another buyer through direct marketing methods such as letters or visits are

² Competition Board decision dated 17.4.2008 and numbered 08-29/352-113.

seen as "active sales". Establishing a point of sales or distribution warehouse in the region of another buyer is also within the scope of active sales. Advertisements or promotions which directly target customers in a region or customer group assigned to another buyer are also among other active sales methods.

(24) On the other hand, fulfilling demands of customers from the region or customer group of another buyer and which are not a result of active efforts by the buyer constitutes "passive sales," even when the buyer delivers the goods to the customer's address. Advertisements or promotions of a general nature in the media will be evaluated among passive sales methods. Internet sales or sales through similar means are also generally passive sales. However, sending e-mails to customers in the exclusive region or customer group of a different buyer will be seen as an active sales method, unless it is requested by the customers concerned. The same approach will also be taken for sales made through catalogs.

(25) The restriction, by a supplier, of distributors/dealers/buyers from making sales on their own websites is a type of passive sales restriction. Within this context, sales made by means of customers visiting the site owned by the dealer or getting in contact with the dealer, or requesting automatic updates from the dealer are passive sales. Whether or not the dealer provides different language options for its website would not affect the passive nature of the sale. In principle, each dealer must have the right to make sales over the internet. The following restrictions, in particular, concerning internet sales, which are considered under passive sales, will take the vertical agreement under examination out of the scope of the block exemption.

- Restriction by an (exclusive) distributor of access to their own website from customers situated in the (exclusive) region of another distributor, or redirection of these customers to the website of the manufacturer or of another (exclusive) distributor,

- Termination of the transaction if the (exclusive) distributor determines that the address is not situated in the (exclusive) region of the distributor, from the address information such as the delivery, postal, credit card, etc. address of the customer,

- Introduction of restrictions on the ratio of internet sales to total sales (excluding where the supplier requires the distributor to make a certain portion of its sales through physical stores in order to protect the efficiency of physical points of sales without preventing internet sales, or where the supplier introduces conditions to ensure that internet sales are in compliance with the general distribution system),

- Having the distributor pay a higher price to the supplier for products it would resell over the internet in comparison to the products to be offered at the physical points of sale.

(26) Under these Guidelines, the restrictions listed above shall be considered as equivalent with restriction of passive sales . First two restrictions concern the restrictions placed upon buyers in relation to the region or customers the contracted goods or services may be sold. Using these restrictions to prevent fulfillment of the demand received from a certain region or customer group over the internet shall be considered a severe restriction. On the other hand, sales by the dealer to the exclusive region of another distributor or to an exclusive customer group over the internet via

promotions or similar methods shall be considered to be active sales, and the prevention of such sales may fall under the scope of the exemption. Internet advertisements aimed at a certain customer group and/or geographical region and (unsolicited) e-mail shall be considered to be active sales. For instance, advertisements aimed at a certain geographical region via third party platforms/marketplaces will be considered active sales to the residents of that region. Similarly, giving an advertisement aimed at a customer group in a certain region by making a payment to a search engine or an internet advertisement provider shall also be considered active sales to the region concerned.

(27) Another restriction is the introductions of limits for the ratio of sales made through the internet channel. Thus, setting maximum sales ratios for the internet channel shall be considered a severe restriction. The last restriction is having the buyer to pay a higher price for products it would offer on the internet compared to the products offered at the physical points of sale. Implementation of different wholesale prices by the provider, either directly or indirectly (for instance, discount systems) shall be assessed within this framework. The supplier acquiring the power to influence the distribution channel choices of the buyer by increasing the gap between these two prices could prevent buyers who wish to sell over the internet from operating in that area. However, the supplier may make a fixed payment to the buyer, independent from the sales revenues and amounts, in order to support the buyer's sales efforts (internet or physical store sales).

(28) On the other hand, the supplier may introduce certain conditions on the use of internet as a sales channels, similar to the ones it may introduce on physical points of sale or on the catalogues in which the advertisements and promotions are published. For instance, the provider may place quality conditions on the website where its products are offered for sale, and it may also impose a condition to offer certain services to the customers shopping over the internet. In the selective distribution system in particular, the supplier may lay down an obligation that distributors own at least one physical point of sales, as well. However, this condition must not seek to foreclose the market to those players who sell exclusively over the internet (*pure players*) or restrict their sales. Other conditions in addition to the above may also be introduced, but the important point to note is that these conditions may not, either directly or indirectly, aim to prevent online sales by the distributor. The justification of the conditions introduced must be objectively concrete, reasonable and acceptable in terms of the factors such as increasing the nature and quality of the distribution, brand image and/or potential efficiency, etc. Similarly, the supplier may demand that the buyer only sell through "sales platforms/marketplaces"³ which fulfill certain standards and conditions. However, this restriction should not aim to prevent distributor's online sales or price competition. As such, a general prohibition of sales over platforms without objective and uniform conditions and justifications in line with the specific characteristics of the product may be assessed as violations.

(29) Due to the differences between the terms of physical sales and online sales, the criteria introduced for these two distribution channels do not necessarily have to be exactly the same; although these criteria must serve the same goal, must ensure comparable results and must be of a nature that confirms the differences stemming

³ "Sales platform/marketplace" concept is used for those platforms which serve as intermediaries for internet sales.

from the nature of the two distribution channels ("principle of equivalency") In other words, the conditions envisaged should not, directly or indirectly, result in the prevention of internet sales. Accordingly, in case the conditions placed by the supplier violate the principle of equivalency and discourage the use of internet, the conditions in question may be considered to be severe restrictions.

(30) In order to consider a region or customer group as exclusive, that region or customer group must receive active sales only from a single buyer or only from the supplier itself. In other words, if the number of undertakings selling to a specific region or customer group is two or more, that region or customer group is no longer exclusive. Any buyer must be able to make active sales to customers in such a "free" region or customer group. As an example, if an undertaking in the position of a supplier assumes a commitment to supply its products to just two undertakings within the borders of the Ankara province and does not allocate customers among these two undertakings in terms of region or customer type, active and passive sales by sellers in other regions to the Ankara region must not be prevented for such an agreement to benefit from the block exemption.

(31) The first exception of article 4.1(b) of the Communiqué includes the wording: "Provided that it does not cover the sales to be made by customers of the purchaser..." Here is what is meant by that statement: The supplier undertaking may only prevent active sales by the buyer. In case any obligation is placed on the buyer concerning active sales made by the customers of the buyer, it would not be possible to benefit from the block exemption. In other words, customers who are not parties to the vertical agreement between the supplier and the buyer and who procure goods and services from the buyer may sell the goods and services concerned to anyone they wish, without regard to any active-passive sales distinction. For instance, let us assume that a dealer sells the products to grocery stores, in accordance with a distribution agreement signed between the producer company in the position of a supplier and the dealer in the position of a buyer. In this case, grocery stores, who are not parties to the agreement, must have the freedom to sell the goods they procured from the dealer actively or passively, in any region they prefer.

(32) In accordance with the second exception specified in article 4.1(b) of the Communiqué, sales to end users by a buyer operating at the wholesale level may be restricted. Introduction of such a restriction is considered necessary to maintain the efficiency of the distribution network and to ensure that goods and services are provided to the consumers at the end points under equal conditions.

(33) The third exception concerns the nature of the "selective distribution system". Article 3 of the Communiqué defines selective distribution system as "a distribution system whereby the provider undertakes to sell directly or indirectly, the goods or services which are the subject of the agreement, only to distributors selected by it, based on designated criteria, and whereby such distributors undertake not to sell the goods or services in question to unauthorized distributors". Especially in the marketing of brand products such as jewelry and perfumery where pre-sales promotion services are essential, physical characteristics of the outlets where such products are sold as well as the knowledge and qualifications of the sales personnel are of vital importance. Suppliers, who do not want such products with a certain brand image to be sold at unsuitable places by personnel with insufficient knowledge and qualifications, generally choose the selective distribution system as a distribution network. In order to

ensure that such products are supplied to the end users in the most efficient way, a requirement may be introduced to ensure that the product is sold exclusively by the members of the selective distribution system.

(34) The last exception listed in article 4.1(b) of the Communiqué concerns the purchase and sales of parts procured with a view to combining them. Restriction, by the supplier, of the buyers' sale of such parts to the competitors of the supplier, which is in the position of producer, is not considered a limitation that would exclude the agreement from the scope of the block exemption. For instance, a television set producer, when selling the parts of the television sets it produces to a buyer, may prevent the buyer from selling such parts to other television set producers (competing undertakings). However, it would not be possible to benefit from the block exemption if the buyer is prevented from selling these products to other undertakings which are not television set producers.

(35) Within the four exceptions specified in article 4.1.(b) of the Communiqué, the an active-passive sales distinction is not observed except for the first one. In other words, where the last three exception provisions are applicable, all active and passive sales by the buyer may be restricted by the supplier.

2.3. Selective Distribution Systems

(36) As stated in article 4.1(c) of the Communiqué, members of a selective distribution system are not prohibited from making active or passive sales to end users. Even if the undertaking in the position of a supplier forms exclusive regions by stating that it would supply goods to a limited number of buyers in a certain region, active or passive sales by the buyers to end users outside the region may not be prevented. In other words, buyers who are members of a selective distribution system may engage in active or passive sales to end users in any region, including through internet channels. However, the supplier may prevent a system-member buyer from changing the location of the point of sale the buyer operates in, or from opening a new point of sale. This is because, as mentioned above, in the selective distribution system, the physical characteristics of the point of sale is the most important factor affecting the success of the distribution system. However, the launching of a website by a system-member buyer for online sales shall not be considered as opening a new physical point of sale. The other regulation which partly opens selective distribution system to competition is included in article 4.1(d) of the Communiqué. Accordingly, undertakings which adopt the selective distribution system may not place an exclusive purchase obligation on the system-member buyers. In other words, system members are not required to procure the products from the supplier; system members may not be prevented from purchasing the products from other member undertakings.

2.4. Other Restrictions

(37) Another regulation concerning supply agreements dealing with products created by the combination of parts is included in article 4.1(e) of the Communiqué. The supply agreement concluded between the supplier selling such parts and the buyer combining the parts to use in production may not prevent the supplier from selling the relevant parts as spare parts to end users or to repairers who are not authorized by the buyer to maintain or repair the relevant goods⁴. As seen here, the restriction in question,

⁴ Competition Board decision dated 15.8.2005 and numbered 05-51/743-201.

unlike those mentioned above, is placed on the supplier by the buyer. An example to this situation may be the relationship between a supplier producing bicycle chains and a buyer which uses these chains in bicycle production. The bicycle producers in the position of the buyer may not prohibit the supplier bicycle chain producer from selling the chains to end users or to unauthorized, i.e. independent, repairers. However, bicycle producer in the position of the buyer may place a requirement on its own repairers to purchase the chains exclusively from itself. Also, the chain producer may be prohibited from selling to other bicycle producers.

3. NON-COMPETITION OBLIGATION

(38) Article 5 of the Communiqué includes arrangements concerning the non-competition obligations that may be placed on the buyers in vertical agreements. Where the buyer is placed under non-compete obligations exceeding the limits allowed under this article, if the provisions of the agreement including those provisions can be separated from the rest of the agreement, these provisions may not benefit from the block exemption; the remaining articles of the agreement may benefit from the block exemption. If the contract provisions which include the non-competition obligation cannot be separated from the other parts of the contract, then the whole agreement falls out of the scope of the block exemption.

(39) Article 3 of the Communiqué defines non-competition obligation as any kind of direct or indirect obligation preventing the buyer from producing, purchasing, selling or reselling goods or services that compete with the goods or services which are the subject of the agreement. In the sense used in the Communiqué, a non-competition obligation is an obligation which specifies that the buyer should not produce the contracted goods or services itself and should not procure them from a source other than the supplier. However, the Communiqué does not make a distinction between the buyer being required to procure all or of the goods or services it needs or resells from the supplier, and the buyer being required to buy most of those goods (more than 80%) from the supplier. In other words, the supplier giving the buyer the opportunity to make a small part (less than 20%) of its purchases from competing undertakings would not prevent the relevant provision to be considered a non-competition obligation. The purchases made by the buyer in the previous calendar year will be taken as the basis in the calculation of these ratios. If the purchases of the buyer in the previous calendar year is not known, an estimate of the total annual requirement of the buyer may be used instead.

(40) The duration of the non-competition obligation on the buyer is particularly important. Non-competition obligations with a duration of more than five years may not benefit from the block exemption, barring the exception stated in paragraph 39 of these Guidelines. Block exemption may not be applied if the duration of the non-competition obligation on the buyer is indefinite, as well. Non-competition obligations which can be implicitly renewed to exceed five years do not fall under the scope of the block exemption, either. However, in cases where the duration does not exceed five years or any extension after five years is only possible via the explicit consent of both parties and where the buyer is not prevented from terminating the non-competition clause at the end of the five year period, the non-competition obligation may benefit from the block exemption. It may be useful to explain the regulations concerning non-competition obligations with an example: A one-year distribution agreement which places the buyer under a non-competition obligation for the duration of the agreement

and which is automatically renewed each year unless one of the parties objects a certain period of time beforehand shall be considered to be of an indefinite duration. However, if the parties must state their explicit consent to each other every year to renew the agreement, then the agreement shall not be deemed to have an indefinite duration. In other words, non-competition obligations based on an arrangement which considers the agreement not renewed as long as the parties do not explicitly inform each other that they wish to extend the agreement within a certain time period shall not be seen as an agreement with an indefinite duration. In calculating the duration of the five-year non-competition obligation, the starting date shall be taken as the date on which the first agreement (dealership agreement) forming the start of the ongoing competition ban between the parties was concluded. The termination date of the non-competition obligation shall be taken to be the date on which all of the dealership, operation, supply, etc. agreements between the parties that include non-competition obligations, as well as all of the usufruct, title deed annotated rent and equipment contracts that affect the duration of the former agreements are terminated. In case usufruct, rent, equipment, etc. contracts are terminated while dealership, operation, supply, etc. agreements are kept; or conversely, in case existing dealership, operation, supply agreements are terminated while usufruct, rent, equipment, etc. contracts are kept and a new agreement in the same nature is signed between the parties, the vertical relationship shall be considered uninterrupted and the five-year period shall be calculated accordingly. Within this framework, while there are no barriers to the parties signing a new agreement, uninterrupted vertical agreements based on non-competition obligations signed between the parties shall not benefit from the exemption if they exceed the 5-year threshold.

(41) According to the provisional article 1 of the Communiqué, for agreements which are in effect on the date this Communiqué is put into force and which include non-competition provisions exceeding the thresholds specified in the Communiqué as of that date, the duration of the relevant obligations must be shortened to the thresholds specified in the Communiqué or below within one year following the effective date of the Communiqué. If, at the end of that one-year period, the duration of the non-competition obligation is not reduced to the thresholds specified in the Communiqué or below, that provision of the agreement, or the whole agreement in case the relevant provision cannot be separated from the other parts of the agreement, will face the risk of violating the Act. If at the effective date of the Communiqué the remaining duration of the non-competition obligation of the agreement is five years or shorter, the agreement shall be valid for this remaining duration, therefore the undertaking does not need to make any amendments.

(42) If it is determined that a non-competition obligation is placed on the buyer exceeding the thresholds specified in the Communiqué and that the article of the agreement containing this obligation can be separated from the other parts of the agreement, then the Board may consider the duration of the non-competition agreement reduced to the maximum threshold specified in the Communiqué. In that case, if the non-competition obligation placed on the undertaking in the position of the buyer has not yet reached the limit specified in the Communiqué, the buyer shall be under the non-compete obligation for that remaining period, i.e. until the upper limit in the Communiqué is reached. If the undertakings has been under the non-competition obligation for a period exceeding that upper limit, the non-competition obligation shall

be rendered void and the undertaking in the position of the buyer shall become fully independent.

(43) Another important point related to non-competition obligations is that there must not exist any contracts –such as loan contracts, equipment contracts, long-term lease contracts– linked with the main agreement between the parties, or any actual situation that may arise in various forms under individual or real rights –such as long-term grant of usufruct rights– which prevent the buyer from terminating the non-competition obligation at the end of the five-year period. For instance, if the supplier has opened a line of credit for the buyer, the repayment of that credit must not be arranged in a way that would prevent the buyer from being relieved of the non-competition obligation at the end of the five year period. The buyer must have the opportunity to pay any remaining credit following the expiration of the five-year non-competition obligation. Similarly, in cases where the supplier provides some equipment to the buyer, the buyer must have the option to acquire this equipment over their market value at the end the five-year non-competition period. In case usufruct and lease contracts are not compatible in terms of duration with dealership, operation, supply, etc. agreements, or in case they are compatible but one of these is terminated before the other, the exemption to be applied to the non-competition obligation may not exceed five years, as well. In this case, the calculation of the five-year period will take into account the date on which the first agreement (the dealership agreement) that started the competition prohibition was concluded and the date on which the vertical relation based on the competition prohibition was terminated.

(44) There is *one* exception to the regulation which prescribes that a non-competition obligation of at most five years may be placed upon the buyer. On the grounds that, where the facility to be used by the buyer in its operations is completely owned by the supplier, the supplier may reasonably disallow the sale of competing goods in its own facility without its consent, any non-competition obligation to be placed on the buyer in such a situation is not subject to a limitation in terms of duration. Accordingly, a non-competition obligation may be placed on the buyer as long as the buyer is using the facility in question. However, in case a facility already owned by the buyer is leased to the supplier or the supplier is granted usufruct rights and the supplier later allows the buyer, which is the real owner of the property, to operate in the facility, this exception will not be applicable. In other words, only if the supplier holds the ownership of the facility through a real or personal right (such as lease, loan of use, *building* and usufruct rights) granted by third parties with no link to the buyer, only then the supplier may place the buyer under a non-competition obligation with a duration longer than five years. Other than this exception, any direct or indirect agreement and/or practice which extends the non-competition obligation beyond the time limit allowed in the Communiqué would be in violation of the Communiqué. This exception introduced in article 5 of the Communiqué is limited, "primarily and specifically," with the acquisition of the use and/or usufruct rights over the immovable falling under the scope of real or individual rights from third parties at the start of the relationship, and the subsequent operation of the facility by the supplier itself or the establishment of dealer relationships with persons with no link to those granting the use/usufruct rights. An extension to the duration of the exemption before the expiration of the five-year exception period is not possible in case of any change concerning the parties to the vertical agreement, such as via termination of operations or acquisition.

(45) In principle, it is not possible to place non-competition obligations on the buyer concerning the period after the termination of the agreement. However, provided certain conditions are fulfilled, non-competition obligations for the buyer may be introduced, for at most one year following the expiration of the agreement. For this, the non-competition obligation must concern goods and services that are in competition with the contracted goods or services, must be limited to the facility or land on which the buyer operated for the duration of the agreement, and must be mandatory for the protection of the know-how transferred to the buyer by the supplier. The use and disclosure of any know how which has not become public knowledge may be prohibited indefinitely.

(46) Another non-competition obligation practice that is not authorized is the prevention of the sales of a certain competitor's products by the members of a selective distribution system. This provision should not be taken to mean that selective distribution and non-competition obligations may not be practiced together. The undertaking in the position of the supplier of a selective distribution system may mandate that selected buyers sell its own products exclusively and refrain from selling any competing products. However, it may not allow the sale of the products of some of its competitors while preventing others from using this system. In other words, in a selective distribution system, non-competition obligations must either cover all competing products or none of them.

4. THERE IS NO PRESUMPTION OF ILLEGALITY OUTSIDE THE SCOPE OF THE BLOCK EXEMPTION COMMUNIQUÉ

(47) Vertical agreements falling outside the scope of the Block Exemption Communiqué are not automatically deemed to be in violation of article 4 of the Act no 4054. However, these agreements may require individual exemption examinations. In case of anti-competitive effects, undertakings may plead an efficiency defense and explain why a specific distribution system creates benefits meeting the conditions listed in article 5 of the Act.

5. NOTIFICATION REQUIREMENT IS REMOVED

(48) With the Act dated 2.7.2005 and numbered 5388, significant amendments were made in those articles of the Act no 4054 concerning the notification obligation. With the above-mentioned amendment, the obligation to notify agreements, concerted practices and decisions of associations of undertakings within the scope of article 4 of the Act to the Board has been removed. In parallel, the practice of imposing fines on undertakings, associations of undertakings and persons in the managing bodies of undertakings for failing to notify agreements, concerted practices and decisions of associations of undertakings within the scope of article 4 of the Act has been abolished.

(49) As a result of the amendment in the Act, the principle of retroactivity was adopted for exemption decisions taken by the Board, thereby eliminating the legal uncertainty concerning the period before the exemption decision. Exemption decisions shall be valid starting from the date the agreement or concerted practice was put into effect or the association of undertakings decision was taken.

(50) In spite of the removal of the notification obligation, for voluntary notifications to be made concerning vertical agreements falling out of the scope of the block exemption communiqué due to the 40% market share threshold, the Notification Form attached to the "Guidelines on the Voluntary Notification of Agreements, Concerted Practices and Decisions of Associations of Undertakings" should be used.

6. PORTFOLIO OF PRODUCTS DISTRIBUTED BY THE SAME DISTRIBUTION SYSTEM

(51) If a supplier company is using the same distribution agreement in the distribution of many products/services, then, due to the market share threshold, some of these groups may benefit from the block exemption while some of them may not. In such a situation, the block exemption shall be applicable only to those products or services below the market share threshold.

(52) For products and services not covered by the Communiqué;

- The agreement shall not benefit from the block exemption, however this shall not mean that the agreement is in violation of the Act,

- In case there exists a restriction which does not fall under the scope of an individual exemption as per article 5 of the Act, it must first be seen whether there are suitable measures that could solve the competition problem within the current distribution system. For instance, removing a restriction that could not be granted an exemption for those product/s not covered by the Communiqué may be regarded among such measures.

- If suitable measures to that effect cannot be taken, the relevant supplier must make other distribution arrangements. For instance, the supplier may prepare a separate agreement for those product(s) not covered by the Communiqué.

7. TERMINATION OF THE EXEMPTION GRANTED BY THE COMMUNIQUÉ

7.1. Withdrawal of the Exemption

(53) All of the agreements which fulfill the conditions specified in the Communiqué are exempt from the prohibition in article 4 of the Act. This is because the Board, when issuing the Communiqué, assumed that any agreement falling within the framework of the Communiqué would meet the exemption conditions listed in Article 5 of the Act. However, there may be some exceptional circumstances where certain vertical agreements fulfill the conditions specified in the Communiqué, yet do not meet the exemption conditions in article 5 of the Act in terms of their effects. Especially where undertakings parties to the vertical agreement hold significant market power and where there are significant barriers to entry, it may be harder for some types of vertical agreements falling under the Communiqué to meet the conditions required for exemption. The Board has been given an important power to be used in such situations: Article 6.1 of the Communiqué states that in case an agreement that has been granted exemption under the Communiqué is found to have effects incompatible with the conditions set forth in article 5 of the Act, then the Board may withdraw the exemption granted to the agreement by the Communiqué. Therefore, where a vertical agreement is no longer capable of meeting the conditions which allowed it to get an exemption due to its effects on the markets at the implementation stage, the exemption

protection granted by the Communiqué may be withdrawn by the Board, even if the agreement was initially prepared in compliance with the Communiqué. In such a situation, before making its final decision, the Board shall request the written and/or oral opinions of the supplier, and the written and/or oral opinion of the buyer in case of agreements including exclusive supply obligations. The board may also request the written and/or oral opinions of the other party to the agreement, and of the relevant third parties. Also, the withdrawal of the exemption shall not be retroactive. Therefore, since the withdrawal of the exemption is not retroactive, the agreement shall benefit from the exemption for the time period until the decision is taken.

(54) Especially in markets where undertakings with significant market power are parties to agreements, practices aimed at the withdrawal of exemption are unavoidably brought into the agenda. However, the market shares of the undertakings parties to the agreement is not the sole decisive factor in determining whether an exemption should be withdrawn. An exemption granted to a vertical agreement concluded by an undertaking in an oligopolistic market where operating undertakings have similar market shares may be withdrawn as well. In such situations, assessments made shall take into certain factors in addition to market shares, such as barriers to entry, characteristics of the relevant product and the degree of the consumers' dependence on that product.

(55) Negative effects of vertical restrictions are increased when a number of suppliers operating within the market arrange their distribution organizations in parallel with the use of similar restrictions. This is known as cumulative effect, and the withdrawal of the exemption may come about due to competitive problems caused by the cumulative effect as well. When entries into the relevant market and the competition within the relevant market are significantly impeded by parallel networks formed by vertical agreements of a similar nature implemented by competing suppliers or buyers, then fulfilling the exemption conditions of article 5 of the Act may become impossible. In such a case, continuing the exemption granted by the Communiqué is out of the question. Agreements that include vertical restrictions with similar effects shall be deemed to be of a similar nature. Types of vertical restrictions which may have similar effects can be grouped under four headings:

- I. Single Brand Group: Restriction types such as non-competition obligations or quantity constraints which limit the orders of the buyer to goods or services provided by a single supplier are in this category.
- II. Limited Distribution Group: Restriction types such as exclusive distribution, selective distribution, exclusive customer groups and exclusive supply obligations which require the supplier to sell its goods or services to a certain number of buyers are in this category.
- III. Resale Price Group: Types of restrictions such as fixed prices, recommended prices, minimum prices and maximum prices which allow the supplier to interfere with the prices to be implemented by the buyer in the resale of the goods and services are in this category.
- IV. Market allocation group: Exclusive region restrictions which force the buyer to purchase certain goods and services from a previously determined supplier or which introduces limits concerning resale regions are in this category.

7.2. Exclusion of Parallel Networks from the Scope of the Exemption

(56) Article 6.2 of the Communiqué gives the Board the opportunity to intervene in a different way when parallel networks become too widespread to be eliminated through a revocation of the exemption. Accordingly, in case vertical agreement networks utilizing similar vertical restrictions cover more than 50% of the market, the Board may issue a communiqué to exclude agreements with certain limitations utilized in the market from the scope of the Communiqué. For instance, this option may be introduced if parallel selective distribution networks have started to cover more than half of the distribution channels within the relevant market, in spite of the fact that the characteristics of the relevant product does not require selective criteria. There are the following differences between the revocation method prescribed under article 6.1 of the Communiqué and the method prescribed under the second paragraph of the same article:

- The revocation method concerns individual agreements between specific undertakings while the method of exclusion from the exemption via a communiqué concerns all undertakings active in the relevant market which implement the agreements defined in the communiqué.

- In the revocation method of article 6.1 of the Communiqué, the revocation decision establishes that article 4 of the Act was violated by certain undertaking(s); whereas, the exclusion from the exemption by a communiqué method of article 6.2 of the Communiqué only eliminates block exemption protection for types of vertical agreements which include specific limitations and opens the way for the application of article 4 and 5 of the Act. In that case, previous decisions of the Competition Board on the subject will be instructive.

(57) The Board shall choose the appropriate method between the revocation method in article 6.1 of the Communiqué and the exclusion from the exemption by a communiqué method in article 6.2 of the Communiqué. Even if the coverage ratio of parallel networks within the relevant market rises above 50%, this does not place the Board under an obligation to implement the exclusion from the exemption by a communiqué method. In addition to the coverage ratio, entries into the market or competition within the market must be significantly restricted due to parallel networks.

(58) When making a decision based on the exclusion from the exemption by a communiqué method, the Board shall consider whether the revocation method might be sufficient and appropriate. Within this framework, the Board shall make an assessment after taking into account the number of competing undertakings contributing to the cumulative effect within the relevant market, and shall decide which method is more suitable accordingly. The Board shall define the scope and framework of the implementation in the communiqué it will issue. A transition period of at least six months is specified for these types of communiqués. Thus, relevant undertakings shall continue to be covered by the exemption during the transition period, and will have the opportunity to review their agreements during that time.

8. MARKET DEFINITION AND CALCULATION OF MARKET SHARES

8.1. Guidelines on the Definition of Relevant Market

(59) "Guidelines of the Definition of Relevant Market," adopted with the decision dated 10.1.2008 and numbered 08-04/56-M, is indicative on subjects related to the definition of the relevant market within the framework of the application of the Board's competition policy. When defining markets, "Guidelines of the Definition of Relevant Market" shall be taken into consideration, and the Guidelines herein shall not go into detail concerning market definition. However, some special circumstances specific to vertical restrictions which are not addressed in the "Guidelines of the Definition of Relevant Market" shall be examined below.

8.2. Establishment of the Relevant Market for the Calculation of the 40% Market Threshold of the Communiqué

(60) According to article 2.2 of the Communiqué, the determinant of the Communiqué's scope is the market share of the supplier. However, this general rule has an exception: In accordance with article 2.3 of the Communiqué, only for vertical agreements which include an exclusive supply obligation, the market share of the buyer becomes determinant in terms of the scope of the Communiqué.

(61) In order to calculate the market share, the relevant market must be established. Accordingly, the relevant product market and the relevant geographic market need to be defined. When defining relevant product market, the market consisting of the goods and services deemed to be the same in terms of intended uses and characteristics by the consumers is taken into account, and other factors that may affect the defined market are also evaluated.

(62) Relevant geographical markets are the regions in which undertakings are active in the supply and demand of goods and services, which are sufficiently homogeneous in terms of competitive conditions, and especially, which can be easily distinguished from neighboring regions since competitive conditions are significantly different.

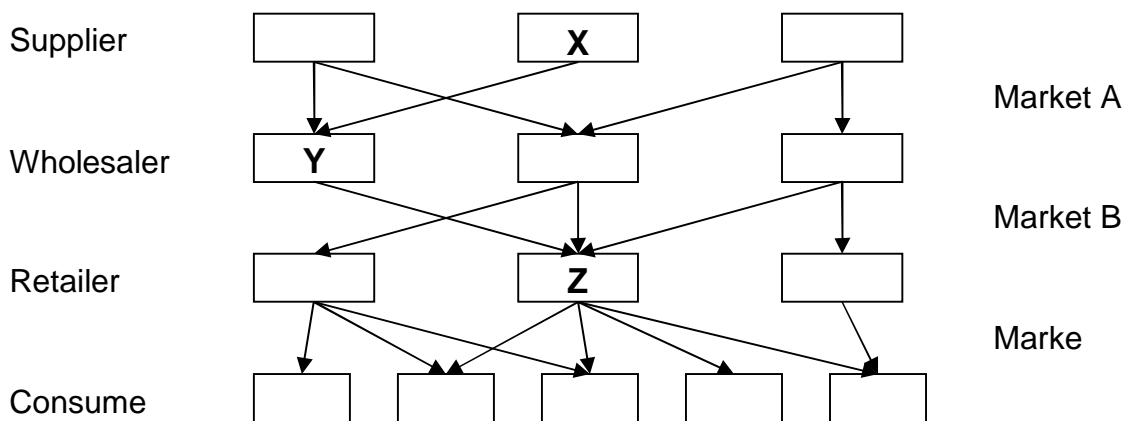
(63) In the application of the Communiqué, the market share of the supplier is its share within the relevant product market and relevant geographical market in which it makes sales to the buyers. In the example given in paragraph 60 below, this market is the Market A. Product market, first of all, is dependent on the substitutability of the product for the buyer. If the product supplied is used as an input in the production of other products and cannot be distinguished in the final product, then the relevant product market is defined based directly on the choices of the buyer. Customers of buyers generally do not have a strong say on the inputs used by the buyers. In general, vertical restrictions between the supplier and the buyer of the input concern the purchase or sale of the intermediate goods and not the sale of the final product. For the distribution of the final product, under the normal circumstances, what is substitutable for the direct buyer will be affected by the choices of the final consumers or will be determined by consumer choice. When purchasing final products as a reseller, a wholesaler/retailer cannot ignore the choices of final consumers. As well, vertical restrictions at the distribution level generally are not limited to the sale of the

product between the supplier and the buyer, but also concern the resale of that product.

(64) In general, when different distribution systems are in competition, markets are not determined in accordance with the distribution type commonly implemented. Where the seller sells a portfolio of products, if the buyers perceive the whole product portfolio as a substitute instead of individual products, then the relevant product market may be defined as the product portfolio in whole.

(65) In the example below, since the buyers (such as Y and Z) in the markets A and B are professional buyers, geographical market is, in general, wider than the market C, where the product is resold to final consumers.

(66) In the following example, in relation to the exclusive supply obligation placed on X by Y, the share of the buyer Y in total purchases in the purchase market (market A) is taken into consideration.



(67) In vertical agreements with three parties where each of the parties operate at a different level (the agreement between X, Y and Z in the example above), the market shares of the parties at both levels must be below the 40% threshold in order for those agreements to benefit from the block exemption. If, for instance, an agreement between a supplier (X), a wholesaler (Y) and a retailer (Z) includes non-competition obligations, for this agreement to benefit from the block exemption, the market shares of the supplier (X) and wholesaler (Y) must not exceed 40%.

(68) If the supplier manufactures both the original equipment and the parts required for the repair or for the spare parts of that equipment, then the supplier generally is the sole or leading supplier in the repair and spare parts market. The same situation may emerge if the supplier (original equipment supplier) contracts the manufacturing of the parts required for repair and spare parts to a sub-contractor. The relevant market established for the application of the block exemption may be defined as the original equipment market including spare parts or separately as an original equipment market and an after-sales market depending on factors such as the effects of the restrictions, lifespan of the equipment and the significance of repair and part replacement costs.

(69) If, in addition to the provision of the contracted products, the vertical agreement also includes provisions concerning intellectual rights to facilitate the marketing of the contracted goods (such as the use of the supplier's trademark), the market share of

the supplier in the market in which it sells the contracted products becomes decisive for the application of the block exemption.

(70) Where a franchisor does not supply goods for resale but provides a range of services together with the intellectual rights constituting the franchised business method, the franchisor must take into account its own market share as the supplier of the business method. To that end, the franchisor must calculate its market share in the market where the business method is used, i.e. the market where the franchisee uses the business method to provide goods or services to the final consumers. The franchisor must calculate its market share based on the value of the goods or services provided by the franchisees in that market. In such a market, competitors may be the other providers of the franchised business method, but other substitute goods and services providers who do not implement the franchising system are also considered competitors. For instance, without prejudice to the definition of such a market, if there exists a market for fast-foods, a franchisor operating in this market must take the relevant sales data of the franchisee in the market when calculating its market share. If the franchisor supplies certain inputs such as meat and spices to the franchisee in addition to a business method, the franchisor must include in its market share calculation its share in the market where these products are sold .

8.3. Relevant Market for Individual Assessment

(71) In the individual assessment of vertical agreements which do not fall under the block exemption, markets other than the relevant market defined for the application of the block exemption may have to be examined. A vertical agreement may affect not only the market between the supplier and the buyer, but also downstream markets. For an individual assessment of the vertical agreement, relevant markets at every trade level affected by the restriction of the agreement shall be evaluated:

(i) For intermediate goods or services integrated by the buyer for its own goods and services, vertical agreements generally affect the market between the supplier and the buyer. For instance, a non-competition obligation placed on the buyer may foreclose the market to other providers, but would not cause a decrease in intra-store competition in the downstream market. On the other hand, in agreements with exclusive supply obligations, the position of the buyer in the downstream market is also important in this context; this is because if the buyer holds market power in the downstream market, any conduct by the buyer to foreclose the market would have significant negative effects in the market.

(ii) For final products, it is not quite possible to limit competition analysis to the market between the supplier and the buyer. This is due to the fact that vertical restrictions may have negative effects in the resale market where the buyer makes its sales, such as a decrease in intra-brand and/or inter-brand competition . For instance, exclusive distribution agreements may not only cause foreclosure effects in the market between the buyer and the supplier, but also may lead to a decrease in intra-brand competition in the regions where the distributors engage in resale. If the distributor sells to final consumers, then the resale market gains particular importance. An agreement between a producer and a wholesaler containing non-competition obligations may foreclose the wholesaler to other producers, but a restriction of intra-brand competition at the wholesaler level does not lead to competitive problems under certain conditions. However, concluding the same agreement with a retailer would lead to a loss of in-

store competition, which would cause a decrease in intra-brand competition at the resale market.

(iii) In the individual assessment of an after-sales market, the relevant market may be defined as the original equipment market or as the after-sales market, depending on the circumstances of the case. For each case, the situation in each separate after-sales market will be assessed in consideration of the situation in the original equipment market. An insignificant market position in the original equipment market would generally mitigate any potential anti-competitive effects in the after-sales market.

8.4. Calculation of Market Share under the Block Exemption Communiqué

(72) As a rule, the market share must be calculated over the sale values in the market. Where sale values are not available, estimations may be made based on credible market data, including sale amounts.

(73) On-site production (undertaking's production of intermediate goods for use in its own production) may be particularly important in competition analysis as a competition restriction or for emphasizing the position of an undertaking within the market. However, on-site production will not be taken into account in the definition of markets and calculation of market shares for intermediate goods and services.

(74) Nevertheless, in dual distribution of final goods, i.e. where the producer of the final product also operates as a distributor within the market, market definition and market share calculation must include the products sold by the producer and the products sold by competing producers through their own connected distributors and agents.

9. IMPLEMENTATION AT THE INDIVIDUAL LEVEL

(75) Agreements between competitors generally lead to harmful effects on the competitive structure. Whereas agreements concluded between undertakings operating at different levels of the "Production-Distribution-Resale" chain are expected to have fewer negative effects on the competitive structure. This expectation is based on a simple economic fact. Undertakings competing at the horizontal level produce substitute products while undertakings in a vertical relationship produce complementary products. Demand for a product falls with the decreases in the price of its substitute, but rises with the decreases in the price of its complementary product. Consequently, in order to sell more, each competing undertakings hopes for a rise in the prices of the others, while undertakings in a vertical relationship wish for a decrease in the prices implemented by each other. As a result, each of the undertakings in a vertical relationship tend to prevent the other from engaging in conduct based on market power.

(76) However, this self-control mechanism of vertical agreements may not always be effective. Undertakings with market power may want to end their conflict of interest with their buyers and maximize their own profit to the disadvantage of their buyers, and as a result, consumers. An undertaking with market power (in the downstream or upstream market) may be able to do this by aligning the independent interests of its buyers with its own interests through vertical restrictions.

(77) Within this framework, in terms of vertical agreements, the application of article 4 of the Act will focus on those undertakings which hold market power. If the undertaking in the case under examination holds significant market power, it becomes important to protect both intra-brand and inter-brand competition.

9.1. The Importance of Intra-Brand Competition

(78) Intra-brand competition is a kind of reaction to market power directed from the upstream towards the downstream and contributes to the development of the competitive process through various ways. Some of these may be listed as:

Arbitrage:

(79) Arbitrators, taking advantage of the consumer demand for a product with market power, help establish the supply and demand equilibrium by engaging in the purchase and resale of the products in accordance with the supply and demand conditions. This not only ensures the most economically efficient distribution of the relevant product the market, but also serves to prevent price discrimination.

Preservation of Efficiency and Innovation in Distribution

(80) Intra-brand competition gives prominence to efficient distributors and resellers, while foreclosing the market to inefficient ones. This situation forces the market players in question to innovate, thereby serving the objective of creating technical and economic development, which is one of the benefits expected from a competitive environment.

Positive Contribution to Competition in the Upstream Market

(81) Intra-brand competition also acts to prevent suppliers from coordinating with other suppliers by enforcing discipline on the prices to remove uncertainties. On the other hand, intense intra-brand competition would have positive effects on competition in the upstream market, since it would force the supplier to compete for access to resellers in the downstream market.

9.2. Negative Effects of Vertical Restrictions

Decrease in Intra-Brand Competition

(82) As much as the restriction of intra-brand competition makes positive contributions to the competition regime through its efficiency increasing aspects, it also can have negative effects due to the elimination of the above-mentioned benefits of intra-brand competition.

Decrease in Inter-Brand Competition

(83) Vertical restrictions have the potential to facilitate undertakings' entering into explicit or implicit collusion. Suppressing intra-brand competition in the downstream market with vertical restrictions support parallel pricing mechanisms in the upstream market, while also allowing suppliers with market power to exercise that power in the downstream markets.

Foreclosure Effect

(84) Market foreclosure effect refers to commercial strategies which restrict the access of the buyer to the supplier and/or of the supplier to the buyer. Market foreclosure effect causes actual and potential competitors to enter downstream and upstream markets simultaneously to ensure vertical integration, or to look for new independent undertakings. Undertakings which implement vertical restrictions thereby increase the costs of their competitors. Besides having negative effects on the existing competition in the market, this situation also prevents potential competition by creating barriers to entry.

Restriction of Consumer Choice

(85) In particular vertical restrictions implemented at the level of regions and customers remove the ability of consumers to choose the best product for themselves and may serve to artificially direct them to certain products.

(86) Vertical restrictions may occur in various types. In order to better examine the effects of vertical restrictions on the market, they must be categorized under two groups: price-related and non-price-related. Price-related vertical restrictions should be examined under four groups: setting maximum prices, setting minimum prices, setting indirect prices and price recommendations; non-price-related vertical restrictions can be examined under three groups: single branding, limited distribution and market allocation. Detailed assessment on each type of vertical restriction listed under the titles above will be examined in detail in the following sections.

9.3. Positive Effects of Vertical Restrictions

(87) Vertical agreements may have an enhancing effect on non-price competition and service quality by increasing the incentives of those players at the lower levels of the production and distribution chain to improve the commercial status of the brand that is the subject of the agreement. This becomes important especially for undertakings without market power, and these undertakings may be left with no way to survive or thrive in the market other than optimizing their production and distribution processes. Especially where specialty products are concerned, agreements which solely specify the terms for purchase and sales of the product may be insufficient to achieve optimal results in the distribution process. In such situations, certain competition restrictions may be utilized in vertical agreements in line with this goal.

(88) This chapter, which aims to give a general and correct idea on the positive effects of vertical agreements, is not a comprehensive list for the aforementioned positive effects. Within this framework, some positive effects which may justify the implementation of vertical restraints are listed below:

(i) Solution of the free riding problem Each distributor dealing with the promotion of the products creates a positive externality on other distributors and the supplier. Other suppliers can take advantage of this positive externality to increase their sales without incurring any cost. In this situation, no distributor would choose to initiate advertisement and promotion activities concerning the product. By implementing

certain vertical restraints, the free-riding problem can be solved and the participation of every distributor in the advertisement and promotion activities may be ensured⁵.

(ii) Entry into new markets: A producer wishing to enter a new market has to make certain choices to be able to launch products or get traction in the market. Since choosing vertical integration by establishing its own distribution network is generally an expensive and inefficient option, producers would want to emphasize promotion and incentive activities in distribution channels comprised of existing distributors. In this case, the producer in the position of the supplier may prefer to allocate a region for the distributor in the position of the buyer and protect it from competition from other distributors for a period of time. Such a protection may also be used to launch a new product via high-prestige distributors to promote a perception of high-quality. Certain vertical restrictions may be imposed in order to ensure that products are sold only at such outlets with a high quality image.

(iii) Solution of the hold-up problem: In some cases, the producer or the distributor may need to make certain specific investments. For instance, the producer may need to build a storage system with certain features specific to the contracted product at the facilities of the distributor. Or, similarly, the distributor may have to make an investment specific to the product or the customer. In such cases, investments need to be directly related to the agreement concerned. Investments to be considered directly related are those which cannot be used by the producer or distributor for any other purpose following the termination of the contract and which can only be sold at a significant loss over its absolute cost, which cannot recoup its own costs in the short term, and which place a burden on one of the parties to the agreement. In order to ensure the recovery of such investments, certain vertical restrictions may be specified.

(iv) Another instance of the hold-up problem may occur where a transfer of know-how is required. If the know-how in question is an essential facility for the implementation of the agreement, then proportionate restrictions on competition which may be introduced for the utilization of such know-how shall not be taken into account under article 4, in general.

(v) Producers may implement certain types of vertical restrictions in order to take advantage of economies of scale by using certain distributors for the distribution of their products, thereby ensuring that end users can access their products at lower prices.

(vi) Undertakings operating in finance markets can propose non-optimal conditions as a result of failures stemming from asymmetrical information. The parties involved in the vertical agreement can eliminate the information as part of the nature of their business and sometimes the producer can extend a loan to the distributor. Certain types of vertical restrictions may be applied where the producers opens a line of credit to the distributor, as well.

⁵ The following may be given as an example for the free-riding problem. In the electronic appliances market where pre-sales services are widespread, consumers may familiarize themselves with electronic appliances in a store where these services are provided, but purchase it cheaper from a store without that service. Since this would lead to a free-riding problem, no buyer would like to provide this service.

(vii) Uniformity and access to quality standards: Vertical restrictions which requires the establishment of certain uniformity and quality standards can help develop the brand image of the contracted products, thereby increasing the perception of quality, and hence demand, for the products.

As observed in the cases summarized above, vertical restrictions implemented under certain conditions can help create economic efficiency and form new markets, leading to positive outcomes which outweigh their negative effects. However, while vertical restraints implemented in cases such as the launch of a product into market or the protection of investments specific to a certain vertical relationship are emphasized by their limited period of validity, certain vertical restraints implemented in some situations can continue for the duration of the agreement.

(89) Most of the vertical restraints examined under section 7.1 can serve as alternatives for each other in the solution of the problems listed above. Selection of the most suitable vertical restraints among the alternatives is important for the analyses to be conducted within the framework of the principle of "not limiting competition more than what is compulsory," set forth in article 5.1(d) of the Act.

9.4. General Rules for the Assessment of Vertical Restrictions

(90) Most significant competition problems related to vertical restraints generally occur when inter-brand competition is insufficient. This insufficiency of inter-brand competition indicates that there is an undertaking upstream which holds market power. It should be noted that the negative effects of vertical restrictions will outweigh its positive effects where problems arising from the insufficiency of intra-brand competition is exacerbated by an insufficiency of inter-brand competition.

(91) Concentration levels in the relevant markets are also important for the assessment of vertical restraints. It can be assumed that vertical restraints other than the hardcore restrictions listed in article 4 of the Communiqué will not lead to negative effects in non-concentrated markets. For the purposes of measuring concentrations, the Herfindahl-Hirschman Index (HHI) is taken as the basis of the calculations. Accordingly, if the HHI is below 1000, it is assumed that the relevant market is not concentrated.

(92) It is possible to compare the negative effects stemming from restrictions of intra-brand competition with the expected positive effects of such agreements and conclude that the positive effects would outweigh the negative ones. However, it is not possible to claim the same in case of vertical agreements which contain restrictions of inter-brand competition. In general, restriction of inter-brand competition leads to more damaging outcomes than the restriction of intra-brand competition. For instance, while it is possible for distribution agreements with non-compete obligations (single-branding) to prevent the access of other brands to the market by giving rise to foreclosure effects, distribution agreements with exclusive region provisions do not hinder the access of consumers to products, even though they may restrict intra-brand competition. However, where inter-brand competition is not sufficient, distribution agreements with exclusivity provisions (concerning regions, customer groups, etc.) can lead to a significant restriction of consumer choice and prevent more economically efficient and innovative distributors from entering the market. This situation would

reduce the drive for innovation in the distribution channel, while eliminating any possibility for consumers to choose after conducting a price-service comparison.

(93) Exclusive arrangements are more harmful for the competitive structure than those without exclusivity. For instance, non-competition obligations force the buyer to purchase from a single brand, while restrictions which are known as quantity forcing and which force the buyer to purchase a certain amount of product make it possible for the buyer to also purchase competing products. Consequently, foreclosure effects created by a restriction in the form of quantity forcing would be relatively smaller.

(94) The existence of brand products increase the possibility of product differentiation and reduces the chances for substitution. This, in turn, can be a factor that facilitates price hikes, since it can reduce the elasticity of demand for the goods and services concerned. For the above-listed reasons, restrictions on competition included in agreements concerning brand goods and services are more harmful than similar restrictions included in agreements concerning non-brand goods and services. The distinction between brand and non-brand goods and services often coincides with the distinction between intermediate goods and services, and final goods and services.

(95) Intermediate goods or services are sold to those undertakings which, in turn, use them as input in the production of other goods and services, and generally they cannot be distinguished in the final goods or services offered. Since buyers of intermediate goods and services have sufficient information, they can assess the quality of goods and services and thus are not reliant on brand and image. Final goods and services, on the other hand, are generally sold to end users who rely more on brand and image. For this reason, prohibition of the sale of certain brands by distributors, who act in accordance with consumer choice, will lead to more harmful outcomes than the prohibition of the purchase of certain brands by undertakings that use intermediate goods. On the other hand, for undertakings buying intermediate goods and services which employ special purchasing departments or consultants in order to follow the developments in the purchase market and which buy at significant volumes, search costs do not constitute a significant barrier. Therefore, a reduction in intra-brand competition at the intermediate goods and services level would lead to fewer competition problems when compared to a similar reduction at the level of final goods or services.

(96) Co-existence of various types of vertical restrictions will generally increase the negative effects of these restrictions. However, in certain situations, combination of certain types of restrictions may lead to more positive outcomes than their individual use. For instance, in exclusive distribution systems, distributors may be tempted to increase prices as intra-brand competition has been reduced. In such cases, the use of other types of restraints such as quantity forcing or maximum price setting may reduce these negative effects.

(97) The closer the connection between vertical restrictions and a know-how transfer, the more likely it is that the restrictions will lead to efficiency increases and will be required to protect the know-how or the relevant investments.

(98) Similarly, the more related certain vertical restrictions are to agreement-specific investments, the easier it will be to find justifications for those vertical restrictions. The

validity of the justifications will depend on the period of time required to recover the investments.

(99) When a new product is launched in the market, or when an existing product is introduced to a different geographical market for the first time, the undertaking concerned may have trouble defining the market, or its market share in the relevant market may tend to be higher. However, since vertical restrictions related to new product markets or expanding geographical markets do not generally have restrictive effects on competition, this situation will not pose a significant problem. This assessment shall hold for all restrictions with the exception of particularly severe ones, for a period of two years following the introduction of the relevant product, irrespective of the market share of the relevant undertaking. In case of expanding into a new geographical market, a prohibition placed on the buyers of the supplier in other geographical markets preventing active or passive sales into the newly-penetrated geographical market will be evaluated within the same framework. In case of new product launches, a restriction on active sales outside of the test market/customer group placed on the distributor assigned to the specified test market or test consumer group will not be considered a violation of article 4, for a period of one year.

9.5. Methodology of analysis

(100) In general, the assessment of a vertical restriction under article 4 of the Act no 4054 involves the following steps:

1. First, depending on the type of the vertical restriction, the undertakings involved need to define the relevant market so that the market share of the supplier or the buyer may be determined.

2. If the market share is below the 40% threshold, the agreement shall benefit from the block exception, providing it does not include any of the prohibited restrictions and meets the rest of the conditions listed in the Communiqué.

3. If the market share is above the 40% threshold, it is necessary to assess whether the agreement meets the criteria listed in article 5 of the Act.

9.5.1. Relevant factors for the Assessment under Article 5 of the Act

(101) When assessing cases where the 40% threshold is exceeded, the Board will conduct a full competition analysis, including the determination of the undertaking's market power. The assessment for the determination of market power will take the following factors under consideration:

- (a) market position of the supplier,
- (b) market position of the competitors,
- (c) market position of the buyer,
- (d) entry barriers,
- (e) maturity of the market,

- (f) level of trade,
- (g) nature of the product,
- (h) other factors.

(102) The effect of each factor on the assessment may vary depending on all other factors and on a case by case basis. For instance, a high market share for the supplier is often a significant indication of market power, however if entry barriers are low, a high market share would not indicate market power. Consequently, it is not possible to provide firm rules on the importance of individual factors.

Market Position of the Supplier

(103) The first and foremost indication of a supplier's market position is its share in the relevant market. The higher their market share, the higher their market power may be. If the supplier has certain cost advantages when compared to its competitors, its market share would be even larger. These competitive advantages may result from various factors, including being a first mover in the market, holding essential patents or having superior technology, being the brand leader or from having a stronger/larger portfolio.

Market Position of the Competitors

(104) The same indicators (market share and competitive advantages) are used for the determination of the market position of the competitors, as well. The stronger the competitors and the greater their number, the less risk there is that the supplier and buyer parties to the agreement will be able to foreclose the market or soften inter-brand competition. However, as the number of competitors decrease and their market position (size, cost, R&D potential, etc.) become more similar, such a market structure will increase the risk of implicit/explicit collusion. Fluctuating or rapidly changing market shares are in general an indication of intense competition.

Market Position of the Buyer

(105) Buyer power is related to the market position of the buyer. The first indicator of buyer power is the market share of the customer in the purchase market. That market share reflects the importance of the buyer's demand for possible suppliers. Other indicators focus on the position of the buyer in the resale market, such as the geographic spread of outlets, brands owned by the buyer/distributor, and its image amongst final consumers. Potential restrictive effects of buyer power on competition may vary depending on the types of vertical restrictions.

Barriers to Entry

(106) Entry barriers are measured by the extent to which incumbent companies can increase their price above the competitive level (generally, minimum average total cost) and by whether they can make abnormal profits without attracting new entry. In the absence of entry barriers, easy and quick entry would ensure that incumbents cannot make abnormal profits. When easy and quick entry into the market that eliminates abnormal profits occurs within one or two years, entry barriers can be said to be low.

(107) Entry barriers may result from a wide variety of factors such as economies of scale and scope, government regulations (especially where they involve exclusive rights, state aid, import tariffs, intellectual property rights, ownership of resources where the supply is limited due to for instance natural limitations), essential facilities, a first mover advantage and brand reliance of consumers created by strong marketing. Vertical restrictions and vertical integration may also work as an entry barrier by making entry more difficult for (potential) competitors and foreclosing the market to (potential) competitors. Entry barriers may be present at only the supplier or buyer level or at both levels.

(108) The question whether the factors listed above should be described as entry barriers depends on whether they entail sunk costs. Sunk costs are those costs are required to enter or be active in a market, but that are lost when the market is exited. Advertising costs to build consumer loyalty are normally sunk costs. However, if an exiting firm can either sell its brand name or use it somewhere else without a loss, then advertising expenditures are excluded from sunk costs. Since sunk costs make it costly for incumbents to leave the market, the more costs are sunk, the more potential entrants may perceive the risk of entering the market and the more credibly incumbents can threaten that they will match new competition. For instance, where distributors are tied to a manufacturer via a non-competition obligation, the foreclosing effect will be more significant if setting up its own distribution system will impose sunk costs on the potential competitor.

(109) In general, entry requires sunk costs, sometimes minor and sometimes major. Therefore, actual competition is in general more effective and will weigh more heavily in the assessment of a case than potential competition.

Maturity of the Market

(110) A mature market is a one where the technology used is well known and widespread and not changing very much, where there are no major innovations and where demand is relatively stable or declining. In such a market, negative effects of vertical restrictions are more likely than in more dynamic markets.

Level of Trade

(111) The level of trade is linked to the distinction between intermediate and final goods. As mentioned before, vertical restrictions are less likely to cause negative effects at the level of intermediate goods. A similar distinction may be made between wholesale trade and retail trade. Vertical restrictions, in general, lead to more negative effects at the retail trade level.

Nature of the Product

(112) The nature of the product plays a role particularly for final products, in assessing both the likely negative and the likely positive effects. When assessing the likely negative effects of vertical restrictions, it is important whether the products on the market are more homogeneous or heterogeneous, whether the product is expensive or not in terms of the place it takes in the consumer's budget, and whether the product is a one-off or repeated purchase. In general, when the product is more

heterogeneous, less expensive and is more of a one-off purchase, vertical restrictions are more likely to have negative effects.

Other Factors

(113) In the assessment of a particular restriction, other factors may have to be taken into account. These factors include the cumulative effect which shows the coverage of the market by similar agreements, the duration of the agreements, whether the agreements are imposed (mainly one party is subject to the restrictions or obligations) or agreed (both parties accept restrictions or obligations), price leadership, pre-announced price changes and discussions on the right price, price rigidity in response to excess capacity, price differentiation, and regulatory framework or behavior which support or facilitate collusion such as past collusive behavior.

(114) Article 5 of the Act states that the Board may exempt agreements and concerted practices of undertakings as well as decisions of associations of undertakings from the application of article 4 of the Act, provided that all of the following conditions are met:

a) Ensuring new developments and improvements, or economic or technical development in the production or distribution of goods and in the provision of services,

b) Benefiting the consumer from the above-mentioned,

c) Not eliminating competition in a significant part of the relevant market,

d) Not limiting competition more than what is compulsory for achieving the goals set out in sub-paragraphs (a) and (b).

(115) The criterion of not eliminating competition in a significant part of the relevant market, set forth in article 5(c) of the Act, is closely linked to market power and to the effect of the relevant agreements on the market depending on that power. As a rule, if the market power of an undertaking is high, a vertical restriction with a significant distorting effect on competition shall not be granted an exemption. However, in case of objective justifications, such as when it is necessary for protecting relationship-specific investments or within the framework of a significant know-how transfer that is not related to the provision of the service or acquisition of the goods, the vertical restriction may be exempted from the scope of article 4 of the Act.

(116) If the supplier and buyer are not in a dominant position, remaining three conditions become more important. The first condition is related to improving production and distribution as well as increasing technical and economic development. These efficiencies must have been realized and must have led to net positive outcomes. Speculative claims such as solution of a free-riding problem or general explanations such as cost-cutting shall not be deemed acceptable. Cost advantages which are caused entirely by market power or anti-competitive behaviors shall not be accepted. Within the context of the second condition, economic benefits must not be only for the parties to the agreement, and they should have advantages for the consumer as well. In general, the level at which benefits are passed on to the consumers is directly tied to the concentration of competition in the market. Normally, competitive pressure leads to cost savings being passed-on to the consumers in the form of lower prices, or it encourages faster introduction of products into the market by

the undertakings. For this reason, if the relevant market has sufficient competition to effectively restrict the parties to the agreement, the competitive process shall normally ensure that the consumers get a fair share of the economic benefits. The last condition listed above plays a role in selecting the restrictions with the least distorting effect on competition in order to achieve various positive outcomes.

9.5.2. Analysis of Various Vertical Restrictions

(117) This chapter will analyze vertical restrictions and their combinations most frequently used by undertakings.

9.5.2.1. Single Branding

(118) Single branding agreements have as their main element the fact that the buyer is encouraged to procure all or most of its requirements for a particular product or group of products from a single supplier. Even where the agreements do not include a provision related to single branding, if the supplier implements certain incentives such as loyalty discounts or target discounts, the agreement shall be assessed within this framework as well. In addition, a similar element may occur in tying agreements where buyers that purchase one product are encouraged or obligated to also purchase another distinct product as a condition for the sale of the former.

(119) Single branding agreements mainly have four negative effects on competition.

(i) Foreclosure effect: Other suppliers cannot sell to certain buyers in the market, which may lead to foreclosure.

(ii) Coordination effect: These agreements cause rigidity in market shares, and will facilitate coordination if implemented by a number of suppliers.

(iii) Prevention of intra-store competition effect: Where distribution of final products is concerned, certain retailers will sell a single brand and therefore there will be no inter-brand competition within the stores of these retailers.

(iv) Costliness effect: In tying agreements, the buyer may have to purchase the product at a higher cost than it would have been able to purchase it from different suppliers, were the tying agreements did not exist. All of these effects cause a decrease in inter-brand competition.

(120) The negative effects of the reduction of inter-brand competition caused by single branding agreements may be mitigated by the fact that the suppliers enter into intense competition at the start of the process to conclude such agreements; however, in case the duration of the non-competition obligation is extended, said mitigation shall not be sufficient to counterbalance the reduction in inter-brand competition.

(121) On the other hand, single branding agreements may also have positive effects on competition. The positive effects of single-branding are as follows:

(i) Solution of the free-riding problem⁶: Single branding facilitates the solution of the free-riding problem. A distributor may take unfair advantage of another distributor's

⁶ See par. 88 (i)

efforts to increase sales. This leads to the problem known as free-riding in the literature. The free-riding problem may also occur amongst suppliers. For instance, when a supplier makes a promotion investment into a retailer, this promotion will also attract its competitors to the same retailer. Introduction of non-compete obligations may eliminate this problem.

Free-riding amongst suppliers will only take place where the promotion is limited to the premises of the retailer and is generic. A free-rider argument will not be accepted in case of a brand-specific promotion.

(ii) Hold-up Problem⁷: Single branding agreements contribute to the solution of the hold-up problem. Hold-up problem occurs in investments specific to the agreement or to the commercial relationship. The nature of these types of investments is that, when they are undertaken by the supplier, they cannot be used to fulfill the needs of other buyers and they lose significant value at resale. Where this problem occurs, the supplier will refuse to invest since it would be unable to depreciate its investment. In order to solve the problem, the supplier may place non-competition or quantity forcing obligations on the buyer. However, the hold-up problem only manifests under certain circumstances. First of all, as mentioned above, the investment must be specific to the buyer. Second, it must be a long-term investment that cannot be recovered in a short period of time. Third, the investment must be asymmetrical; in other words, one of the parties to the agreement must have invested more than the other. In case all of these conditions are fulfilled, the aforementioned competition restrictions may be placed on the buyer for the purposes of investment depreciation.

(iii) Know-how transfer: A particular type of hold-up problem may occur during know-how transfers. Once transferred, it is not possible to withdraw know-how and the supplier transferring the know-how would not want it to be used by or for its competitors. Non-competition obligations may be justified where the know-how is difficult to obtain by the buyer and it is fundamental and essential for the functioning of the agreement.

(122) The Communiqué exempts single branding agreements (like non-competition and quantity forcing agreements), provided that the market share of the supplier is below 40% and the duration of the restraint in question is no longer than five years. Where the market share is above 40% or the time limit is longer than five years, the following points should be taken into account for individual assessments.

(123) "Market position of the supplier" is one of the most important factors in determining the anti-competitive effects of the non-competition obligation on the market. Generally, such obligations are introduced by the suppliers, and the supplier also signs similar agreements with other buyers.

(124) In addition to the market position of the supplier, the scope and duration of the non-competition obligation are particularly important for the assessment in question. As the sales of the supplier arising from the single branding agreement increase, in other words, as the tied market share increase, so will the risk of market foreclosure. Similarly, as the duration of the non-competition obligation increase, so will market foreclosure. It is accepted that agreements which are concluded by non-dominant

⁷ See par. 88(iii)

undertakings with a duration of less than one year are less likely to distort competition to an appreciable extent. Non-dominant undertakings may obtain exemptions for their agreements containing non-competition obligations of one to five years only if a balance is reached between the anti-competitive and pro-competitive effects of these agreements. On the other hand, similar agreements with a duration of more than five years are considered to be non-essential for obtaining the efficiencies claimed for most types of investments, or these efficiencies are not sufficient to counterbalance the foreclosure effect.

(125) "Market position of competitors" is also important when evaluating the market power of the supplier. If the competitors are of a sufficient number and strong, then the single branding agreement concluded by the supplier is not expected to have appreciable anti-competitive effects. Foreclosure effect may arise if competitors are significantly smaller than the supplier implementing the single branding agreement. If the competitors are similarly sized and if they offer similarly attractive products, market foreclosure may not occur. However, if suppliers have signed similar agreements with a large number of buyers in the relevant market, the market may be foreclosed to potential competitors. This situation, known as cumulative effect, may also lead to collusion amongst suppliers. If the suppliers are covered by the Communiqué, the exemption may have to be withdrawn in order to eliminate cumulative effects of this kind. If the tied market share of a supplier is less than 5%, it may be assumed that the relevant supplier does not make a significant contribution to the cumulative foreclosure effect.

(126) Where the market share of the largest supplier is below 40% and total market share of the four largest undertakings (CR4) is below 50%, single or cumulative restriction of competition will not be a concern. Therefore, failure of successful entry by a new undertaking will arise not from single branding agreements, but from other factors such as consumer choice. If inter-brand competition is intense, i.e. if several undertakings are in intense competition in the relevant market, competition problems related to single branding agreements are not likely.

(127) Entry barriers are important to establish whether there is anti-competitive foreclosure. Where it is relatively easy for competing suppliers to create new buyers or find alternative buyers for their product, foreclosure will not be an issue. However, there are often entry barriers, both at the manufacturing and at the distribution level.

(128) Buyer power (countervailing power) is also relevant in this assessment. Powerful buyers will not be easily discouraged from selling competing goods or services. Foreclosure outcomes which are not based upon efficiencies and which have harmful effects on the consumers can be a significant risk, particularly where the buyers are scattered. However, non-competition agreements signed with major buyers can lead to a strong foreclosure effect.

(129) Lastly, "the level of trade" is relevant in terms of foreclosure effects. Market foreclosure is less likely in case of intermediate products. When the manufacturer of an intermediate product is not dominant, the competing suppliers will continue to provide a substantial part of the demand that is free. Below the level of dominance, a foreclosure effect for actual and potential competitors may only arise in a cumulative effect situation. A significant cumulative effect is unlikely to arise as long as the tied portion of the market is below 50%. If the supplier is dominant, an obligation to buy all

or a large portion of the product from the supplier may lead to significant market foreclosure. The larger the level of dominant position, the higher the risk of anti-competitive foreclosure.

(130) Where the agreement concerns the sale of final products at the wholesale level, encountering competitive problems below the dominant position level depends on the type of wholesaling and on whether there are entry barriers at the wholesale level. There is no real risk of foreclosure effects, if competing manufacturers can easily establish their own wholesale systems. Whether entry barriers are low depends, in part, on the type of wholesaling, that is, if wholesalers can operate efficiently (profitably) with only the product concerned by the agreement (for example ice cream), they can easily establish their own distribution systems. However, if they can only become efficient (profitable) when they sell a group of products (for example frozen foodstuffs), it is not efficient for the supplier to set up its own wholesaling operation. In that case, anti-competitive effects may arise, even below the level of dominance. In addition, under the above-mentioned entry barriers, cumulative effects may arise if some suppliers tie most of the available wholesalers.

(131) It is more likely for foreclosure effects to occur at the retail level compared to the wholesale level. This is because entry barriers are too high to allow suppliers to set up retail stores for their own products. Besides, non-competition obligation at the retail level leads to the restriction of inter-brand competition by preventing in-store competition. It is for these reasons that significant competitive problems may arise if a non-dominant supplier for final products at the retail level ties more than 30% of the relevant market. Competition in the relevant market is likely to be restricted when a dominant undertaking ties even a small portion of the market by single branding agreements. As the level of dominant position increase, so will the risk of market foreclosure for competitors⁸.

(132) A cumulative foreclosure effect may also arise at the retail level. If all of the undertakings have market shares below 40%, and the total tied market share is below 50%, a cumulative foreclosure effect is unlikely and therefore the block exemption will not be withdrawn. The aforementioned figures may be higher when other factors like entry barriers and the number of competitors are taken into account. Where one of the undertakings have a market share above 40% but is not dominant and if the total tied market share is below 40%, a cumulative foreclosure effect is unlikely.

(133) Where the buyer operates from premises and land owned by the supplier or leased by the supplier from a third party not connected with the buyer, it may be said that a significant competitive problem would not arise below the dominant position level due to the nature of the relationship, even if a foreclosure effect may occur.

(134) In certain sectors, the selling of more than one brand from a single site may be difficult or legally prohibited⁹, in which case a foreclosure problem can be mitigated by limiting the duration of contracts.

⁸ Competition Board decisions dated 22.4.2005 and numbered 05-27/317-80, dated 10.9.2007 and numbered 07-70/863-326, dated 10.09.2007 and numbered 07-70/864-327, dated 15.5.2008 and numbered 08-33/421-147.

⁹ For instance, the Petroleum Market Law no 5015 introduced a single branding obligation on the dealer.

(135) A so-called ‘English clause’, requiring the buyer to report any better offer to the supplier and allowing the buyer only to accept such an offer when the supplier does not match it, can be expected to have the same effect as a non-competition obligation, especially when the buyer has to reveal who makes the better offer. This clause can also increase transparency in the market and, thus, encourage collusion amongst suppliers. An English clause can also function as quantity forcing. Quantity forcing is a weaker form of non-competition obligations. Accordingly, the incentives or obligations agreed upon between the supplier and the buyer forces the buyers to procure a significant portion of their demand from the supplier. Quantity-forcing may take the form of minimum purchase requirements or non-linear pricing, such as conditional rebate schemes, loyalty rebate schemes or a two-part tariff (fixed fee plus a per-unit price). Quantity forcing agreements lead to foreclosure effects that are similar to but weaker than non-competition agreements.

(136) In case of restrictive effects on competition falling under article 4 of the Act, an exemption assessment shall be conducted in light of the conditions listed in article 5 of the Act. Assessment of non-competition obligations specifically looks for relevant efficiency gains.

(137) In the case of a customer-specific investment made by the supplier, the provisions of a non-competition or quantity forcing agreement may fulfill the conditions of article 5 of the Act concerning the period of depreciation of the investment. In the case of high relationship-specific investments, a non-competition obligation exceeding five years may be justified. A relationship-specific investment could, for instance, be the installation or adaptation of equipment by the supplier. The equipment in question must be used afterwards only to produce components for a particular buyer. General or market-specific investments in (extra) capacity are normally not customer-specific investments. However, where a supplier creates new capacity specifically linked to the operations of a particular buyer, this may be considered to be customer-specific. For instance, if a company producing metal cans creates new capacity on the premises of or next to the canning facility of a food producer, and if this new capacity may only be economically viable when selling to this particular customer, the situation will indicate a customer-specific investment.

(138) Where the supplier provides the buyer with a loan or with equipment which is not relationship-specific, this relationship in itself is not sufficient to justify the exemption of a foreclosure effect. It is only more economical for the supplier of a product than for a bank to provide a loan in case of capital market imperfection. However, in such a situation of imperfect capital markets where it is more efficient for the supplier to provide the loan, any non-competition obligation tied to the loan extended will only be justified if the buyer is allowed to terminate this obligation without facing any penalties and to repay the outstanding part of the loan at any point in time. This means that the repayment of the loan should be restructured with equal or decreasing installments, should not be increased in time, and the buyer should be able to purchase the equipment provided by the supplier over its market value. An example for this kind of loan restructuring is when, following the establishment of a new distribution outlet, repayments of a loan may be delayed for one to two years until the sales are at a certain level.

(139) A know-how transfer, such as a franchising agreement, may generally justify a non-competition obligation for the duration of the supply agreement.

(140) Below the level of dominance, the combination of non-competition obligations with exclusive distribution can justify a non-competition obligation that is valid throughout the duration of the agreement. In this case, the non-competition obligation will help the exclusive distributor to improve its distribution efforts within its own region.

Example of Non-Competition Obligation

(141) Let us assume that there is a market leader in the national market for an impulse consumer product, with a market share of 45%. This firm sells most of its products (80%) through tied retailers (tied market share 36%). The relevant agreements oblige the retailers to purchase only from the market leader for at least four years. This undertaking is especially strongly represented in the more densely populated cities. Some of its 10 competitors are active only locally, and the largest competitor has a market share of 12%. Competing undertakings supply only 10% of the market via tied retailers. There is strong brand and product differentiation in the market. The market leader has the strongest brands and it is the only one with regular national advertising campaigns. It provides its tied retailers with special cabinets for displaying its product.

(142) Within the framework of the information above, in total 46% (36% + 10%) of the market is foreclosed to potential competitors and to incumbent firms without tied retailers. It is even more difficult for potential competitors to find entry into the densely populated areas (although this is where the competitors would especially prefer to enter the market). In addition, owing to the strong brand and product differentiation and the high search costs relative to the price of the product, the absence of in-store competition will lead to a loss of welfare for consumers.

(143) The market leader may claim that outlet exclusivity reduces transport costs and prevents hold-up problems concerning the cabinets, thus leading to increases in efficiency. However, the relevant efficiency claims are limited and are not sufficient to outweigh the negative effects on competition. This is because the transport costs are linked to quantity and not exclusivity. As well, the cabinets do not contain special know-how and are not brand specific. Accordingly, in this example, the exemption conditions are not fulfilled.

Example of Quantity Forcing

(144) A producer X with a 45% market share sells 70% of its products through resellers and has signed agreements which specify that these resellers are required to purchase at least 75 % of all of their requirements for that type of product from X. In return, X is offering financing and equipment at favorable rates. The agreements have a duration of five years, in which repayment of the loan is foreseen in equal instalments. However, after the first two years buyers have the option to terminate the agreement with a six-month notice period, if they repay the outstanding loan and take over the equipment at its market value. At the end of the five-year period the equipment becomes the property of the buyer. There are 10 competitors, most of them small, with the biggest having a market share of 20%. Most competing businesses operate through similar agreements with different durations. The producers with market shares below 10% often have agreements with longer durations and with more severe termination clauses. The contracts of producer X leave buyer free to supply 25% of their requirements by competitors. In the last three years, two new producers have

entered the market and gained a total market share of 8%. Part of this market share was acquired by taking over the repayments of resellers in return for agreements.

(145) Producer X's tied market share ($0,75 \times 0,7 \times 0,45$) is around 24%. The other producers' tied market share is 25%. Therefore, in total 49% of the market is foreclosed to potential competitors and to existing competitors without tied outlets for at least the first two years through the supply contracts. The market shows that the resellers often have difficulty in obtaining loans from banks and are too small in general to obtain capital through other means like the issuing of shares. In addition, producer X is able to demonstrate that concentrating its sales on a limited number of resellers allows it to plan its sales better and to save transport costs. In the light of the 25% non-tied part in the contracts of producer X, the possibility for early termination of the contracts, the recent entry of new producers and the fact that around half the market is not tied, it seems likely that the quantity forcing provisions in the agreements of producer X would fulfil the exemption conditions.

9.5.2.2. Exclusive Distribution

(146) In an exclusive distribution agreement, the supplier agrees to sell its products to only one distributor for resale in a particular region. At the same time, active sales by the distributor into other exclusively allocated regions are restricted. The potential competitive risks in an exclusive distribution agreement are mainly reduced intra-brand competition and market partitioning, which may facilitate price discrimination. When most or all of the suppliers apply exclusive distribution, this may facilitate collusion, both at the suppliers' and distributors' level.

(147) Exclusive distribution is automatically exempted by the Communiqué as long as the supplier's market share does not exceed 40%, even if combined with other competition restrictions such as non-competition obligations limited to five years, quantity forcing or exclusive purchasing. Distribution systems which combine exclusive distribution and selective distribution are also exempted by the Communiqué, provided active sales in other regions are not restricted. The following provisions will provide guidance for the individual assessment of exclusive distribution agreements where the market share is above 40%.

(148) The market position of the supplier and its competitors is of major importance in this assessment. This is because the loss of intra-brand competition will be problematic where inter-brand competition is limited. The stronger the position of the supplier, the more problematic is the loss of intra-brand competition. Above the 40% threshold, there may be a risk of a significant reduction in intra-brand competition. An exemption may be granted, provided real efficiencies counterbalance the loss of intra-brand competition.

(149) The position of the competitors can have a dual significance. The presence of strong competitors generally means that the reduction in intra-brand competition may be balanced by sufficient inter-brand competition. However, if the number of competitors is small and their market position is rather similar in terms of market share, capacity and distribution network, there is a risk of anti-competitive collusion. The loss of intra-brand competition can increase that risk, especially in relation to multiple exclusive distribution, which is when different suppliers appoint the same exclusive distributor. If a dealer is granted the exclusive right to distribute two or more close and

important competing products in the same region, inter-brand competition may be substantially restricted. The higher the cumulative market share of the brands distributed by the multiple distributor, the higher the risk of collusion the more inter-brand competition will be reduced. Such cumulative effect situations may be a reason to withdraw the benefit of the Communiqué, if the market shares of the suppliers are below the threshold set out in the Communiqué.

(150) Entry barriers that may hinder suppliers from creating new distributors or finding alternative distributors are less important in assessing the possible anti-competitive effects of exclusive distribution. Foreclosure of other suppliers is only a concern where exclusive distribution is combined with single branding. This is because in such a situation, the only distributor of a product in a certain region may be unable to sell competing products due to non-competition obligations. However, for assessments on this matter, the explanations given above will provide guidance concerning single branding restrictions.

(151) Foreclosure of other distributors is not an issue if the supplier implementing the exclusive distribution system appoints a high number of exclusive distributors in the same market and those exclusive distributors are not restricted in selling to other distributors outside the network. However, foreclosure of other distributors may become an issue where there is buying power and market power downstream, in particular in the case of very large regions where the exclusive distributor becomes the only buyer for a whole market. An example would be a supermarket chain which becomes the single distributor of a leading supplier on the Turkish food retail market. The foreclosure of other distributors may be aggravated in the case of multiple exclusive distribution. If the market shares of each supplier is below the threshold specified by the Communiqué, such a situation may lead to the withdrawal of the benefit of the Communiqué for those agreements.

(152) If exclusive distribution arrangements are imposed on one or more suppliers by significant buyers which are probably situated in different regions, buyer power can increase the risk of collusion by buyers as well.

(153) Maturity of the market is also important in the competitive assessment of exclusive distribution. To wit, loss of intra-brand competition and price discrimination may be a more serious problem in a mature market, but that risk would be smaller in a market with growing demand, changing technologies and changing market positions.

(154) In this analysis, the level of trade becomes important, as the possible negative effects may differ between the wholesale and retail levels. Exclusive distribution is mainly applied in the distribution of final goods and services. A loss of intra-brand competition is especially likely at the retail level, if coupled with large regions. This is due to the fact that final consumers may be confronted with little possibility of choosing between a high price/high service and a low price/low service distributor for an important brand.

(155) Even if a producer assigns very large regions to a distributor at the wholesale level (such as assigning just two exclusive distributor for all of Turkey), as long as the producer is not dominant and the distributor can sell the products to retailers without any limitations, there are not likely to be appreciable restrictive effects on competition.A

possible loss of intra-brand competition at the wholesale level may be easily outweighed by efficiencies obtained in logistics, promotion etc.

(156) When exclusive distribution is combined with single branding, foreclosure of other suppliers may be a concern, especially when exclusive distributors with small regions form a dense network or in case of a cumulative effect. This would require the application of the principles on single branding set out above. However, as long as the combination does not lead to significant foreclosure, the combination of these restrictions may be pro-competitive by encouraging the exclusive distributor to focus on a certain brand. Therefore, in the absence of such foreclosure effects, the combination of exclusive distribution with non-competition for the whole duration of the agreement may allow the application of the exemption, particularly at the wholesale level.

(157) The combination of exclusive distribution with exclusive buying may reduce intra-brand competition and increase the risk of market partitioning which may facilitate price discrimination in particular. Exclusive distribution already limits arbitrage by customers by limiting the number of distributors, and usually also restricts the distributors in their freedom of active selling. Exclusive buying requires exclusive distributors to source their supplies for a particular brand directly from the producer. Thus, exclusive buying obligations eliminate arbitrage opportunities by preventing exclusive distributors from buying from other distributors in the system. This allows the supplier to limit intra-brand competition while applying dissimilar conditions of sale. When the market share of the supplier is above 40%, granting exemption to the combination of these restrictions requires the existence of clear and fundamental efficiency increases.

(158) The nature of the product is not important for the assessment of possible anti-competitive effects of exclusive distribution. However, it may become relevant to a discussion of possible efficiency increases, following the establishment of significant restriction of competition caused by exclusive distribution.

(159) Exclusive distribution may lead to efficiencies, especially where investments by the distributors must be protected or the brand image must be established. In general, the case for efficiencies is strongest for new products, complex products, experience products whose qualities are difficult to judge before consumption or those products which are difficult to judge even after consumption.

Example of Multiple Dealership in an Oligopolistic Market

(160) In a national market for a final product, there are four undertakings, each with a market share of around 20%. These undertakings sell their product through exclusive distributors at the retail level. Distributors (retailers) are assigned an exclusive region corresponding to a town or a district of the town for large towns. In most regions, the four firms in question utilize the same retailer (multiple dealership). The remaining 20% of the market is composed of small local producers, the largest of which have a market share of 5%. Those local producers sell their products through other retailers, because the retailers working with the market leaders show little interest in selling these less well-known brands with no market power. There is strong brand and product differentiation in the market. The four producers have national advertising campaigns for their products, whereas this is not the case for the local producers. The market

displays a stable structure. In addition there are no major product and technological innovations within the market. The product is relatively simple.

(161) In such an oligopolistic market, there is a risk of collusion between the four companies. That risk will increase if the firms utilize the same dealers for distribution (multiple dealerships). Regional exclusivity also serves to limit intra-brand competition. Since the retailer sets the price of all four brands in each region, competition between the four producers will be reduced at the retail level. Under multiple dealership, if one producer cuts its prices, the retailer will not transmit this price cut to the consumer. This is because if the retailer cut the prices for that brand, this would reduce its sales, and thus profits, for the other brands. Hence, producers will have reduced incentives to enter into price competition. Inter-brand price competition will exist only with the local producers with low brand recognition. The possible efficiency increases for this multiple exclusive dealership system is limited, as the product is relatively simple, and thus resale does not require any specific investments or training, and advertising activities for the product is carried out by the producers.

(162) In the example given above, the exemption may be withdrawn from these agreements despite the fact that all four companies are below the market share threshold, since the exemption criteria of article 5 of the Act have not been fulfilled.

9.5.2.3. Exclusive Customer Allocation

(163) In an exclusive customer allocation agreement, the supplier agrees to sell its products to only one distributor for resale to a particular group of customers. At the same time, it is usually prohibited for the distributor to make active sales to other, exclusively allocated groups of customers. The possible competition risks that may arise as a result of the limitation concerned are mainly reduced intra-brand competition and market partitioning that may lead to price discrimination. Where most or all of the suppliers implement exclusive customer allocation agreements, the risk of anti-competitive collusion, both at the suppliers' and the distributors' level, will be increased.

(164) Exclusive customer allocation is exempted by the Communiqué when the supplier's market share does not exceed the 40% threshold, even if combined with other competition restrictions such as non-competition obligations, quantity-forcing or exclusive sourcing. The combined implementation of exclusive customer allocation with selective distribution is a violation that is clearly excluded from the scope of the Communiqué, since restricting active sales by appointed distributors to end users is not generally allowed. If the market share threshold is exceeded, an assessment shall be conducted in accordance with the special provisions set out in these Guidelines.

(165) Exclusive customer allocation complicates arbitrage by its nature. In addition, as each appointed distributor has its own class of customers, non-appointed distributors not falling within such a class may find it difficult to obtain the product. Consequently, the possibility of arbitrage by non-appointed distributors will be reduced. Within this context, when assessing exclusive customer allocation agreements concluded by undertakings above the 40% market share threshold, outcomes with clear and fundamental efficiencies becomes particularly important. In the absence of such efficiencies, individual exemption will be out of the question.

(166) Exclusive customer allocation is mainly applied to final products at the wholesale level, where customer groups with different specific requirements concerning the intermediate goods and the product can be distinguished.

(167) Exclusive customer allocation will lead to efficiencies especially when the distributors need to make investments in specific skills and know-how in order to meet the requirements of the undertakings within their class of customers. The depreciation period of these investments has a decisive role in the duration of the exclusive customer allocation agreement. In general the case is strongest for new or complex products and for products requiring adaptation to the needs of the individual customer. Identifiable differentiated needs are more likely for intermediate goods where the product is sold to different types of professional buyers. Exclusive allocation of final consumers is unlikely to lead to efficiencies and therefore such agreements are unlikely to benefit from exemption.

Example of Exclusive Customer Allocation

(168) An undertaking has developed a sophisticated sprinkler system for fire suppression. The company has currently a market share of 45% in the market for sprinklers. When it started selling this new product, it had a market share of 20% with an older product. The installation of the new system depends on the type of building that it will be installed in (office, chemical plant, hospital etc.). The company has appointed a number of distributors to sell and install the sprinkler systems. Each distributor needs to train its employees for the general and specific requirements of the installation of the sprinkler system for a particular class of customers. In order to ensure specialization, the undertaking assigned to a distributor to each exclusive class of customers and prohibited active sales to each others' customer groups. After five years, the active sales restriction will be removed and all exclusive distributors will be allowed to sell to all groups of customers, thereby ending the system of exclusive customer allocation. The supplier may then also start selling to new distributors. The market is a dynamic one, with two recent entries and a number of technological developments. Competitors, with market shares between 25% and 5%, are also developing their own products.

(169) In this example, as the exclusivity is of limited duration and helps distributors recoup their investments and concentrate their sales efforts first on a certain group of customers in order to learn the trade, and as the possible anti-competitive effects are limited in a dynamic market, the conditions of exemption are likely to be fulfilled.

9.5.2.4. Selective Distribution

(170) Selective distribution agreements, like exclusive distribution agreements, restrict the number of authorized distributors on the one hand and the possibilities of resale on the other. The difference with exclusive distribution is that the restriction of the number of dealers does not depend on the number of regions but on selection criteria determined in accordance with the nature of the product. Another difference is that the restriction on resale is not a restriction on active selling to an exclusive region, but a restriction on any sales to non-authorized distributors. In other words, in these types of agreements, sales can only be made to appointed dealers and final customers. Selective distribution is almost always used to distribute branded final products.

(171) The possible competition risks of selective distribution are a reduction in intra-brand competition, foreclosure of certain type of distributors, especially in case of cumulative effect, and facilitation of collusion between suppliers or buyers. To assess the possible anti-competitive effects, a distinction needs to be made between qualitative selective distribution and quantitative selective distribution. In purely qualitative selective distribution, distributors are selected on the basis of objective criteria required by the nature of the product such as training of sales personnel, the service provided, a certain range of the products being sold, etc. The application of these criteria does not impose a direct limit on the number of distributors. Purely qualitative selective distribution is in general considered to fall outside article 4 of the Act for lack of anti-competitive effects, provided that following three conditions are satisfied. First, the nature of the product in question must necessitate a selective distribution system, in order to preserve its quality and ensure its proper use; that is, a legitimate requirement must exist owing to the nature of the product. Secondly, resellers must be chosen on the basis of objective criteria of a qualitative nature. These criteria must be laid down uniformly for all potential resellers and in a non-discriminatory manner. Thirdly, the criteria laid down must not go beyond what is necessary. Quantitative selective distribution, on the other hand, refers to a system with certain additional criteria that limit the potential number of direct sellers, such as minimum or maximum sales clauses or direct determination of the number of sellers.

(172) Qualitative and quantitative selective distribution may benefit from the block exemption up to the 40% market share threshold, even if combined with other non-hardcore restraints, such as non-competition or exclusive distribution, provided active selling by the authorized distributors to each other and to end users is not restricted. The Communiqué grants exemption to selective distribution networks, regardless of the nature of the product. However, where the nature of the product does not require selective distribution, such a system does not generally bring about sufficient efficiencies to counterbalance a reduction in intra-brand competition. Where the selective distribution agreement is found to have effects incompatible with the provisions set out in article 5 of the Act, the exemption may be withdrawn. The following points will provide guidance for selective distribution agreements where the supplier's market share exceeds 40% or in the case of cumulative effects resulting from parallel networks.

(173) The market position of the supplier and its competitors is of central importance in assessing possible anti-competitive effects, since the loss of intra-brand competition can only be problematic if inter-brand competition is limited. As the provider's power increases, the reduction in intra-brand competition becomes a larger problem. Another important factor is the number of selective distribution networks present in the market. Quantitative selective distribution systems applied by one non-dominant supplier in the market cannot normally create net negative effects under the normal circumstances. That point is true as long as the contract goods, having regard to their nature, require the use of a selective distribution system and the criteria applied are necessary to ensure efficient distribution of the goods in question.

(174) The position of competitors has a dual significance and plays a particular role in cumulative effects analysis. Strong competitors will indicate that the reduction in intra-brand competition can be easily counterbalanced by sufficient inter-brand competition. However, where a majority of the main suppliers apply selective distribution, there will

be a significant loss of intra- brand competition, a risk of possible foreclosure of certain types of distributors will be created and the risk of anti-competitive collusion between those suppliers will increase. The possibility of foreclosure of efficient distributors is greater with selective distribution than with exclusive distribution, since sales to non-authorized distributors are restricted. That system gives selective distribution systems a closed character, by making it impossible for non-authorized distributors to obtain supplies. This closed distribution system may serve to reduce the incentives for producers and distributors to lower their prices by sacrificing their profits.

(175) Where each parallel network of a selective distribution system benefits from the Communiqué, The Board may withdraw the exemption with a Communiqué in case of cumulative effects. However, a cumulative effect problem will not arise when the share of the market covered by all of the selective distribution systems in the market is below 50%. Also, no problem is likely to arise even where the market coverage ratio exceeds 50%, as long as the market shares of the five largest suppliers (CR5) is below 50%. Where both the CR5 and market coverage exceed 50%, the assessment may vary depending on whether or not all five largest suppliers apply a selective distribution system. The stronger the position of the competitors which do not apply selective distribution, the less likely other distributors will be foreclosed. If all five largest suppliers apply selective distribution, competition concerns may arise with respect to those agreements in particular that limit the number of authorized sellers by applying quantitative selection criteria. If selective distribution systems prevent access to the market by new distributors capable of successfully selling the products in question especially by utilizing price discounts, thereby limiting distribution to the advantage of certain existing channels and to the detriment of final consumers, an exemption within the framework of article 5 of the Act will not be granted. More indirect forms of quantitative selective distribution, resulting for instance from the combination of purely qualitative selection criteria with the requirement imposed on the sellers to achieve a minimum amount of annual purchases, are less likely to produce net negative effects. However, the amount established for such an annual purchase target should not represent a significant proportion of the seller's total annual sales achieved with the type of products in question and it should not go beyond what is necessary for the supplier to recoup its relationship-specific investment and/or realize economies of scale in distribution. Suppliers with a market share of less than 5% are in general not considered to contribute significantly to a cumulative effect.

(176) Entry barriers are mainly intended to foreclose the market to non-authorized dealers. In general, entry barriers becomes important where selective distribution is applied by manufacturers of branded products. It will take time for distributors excluded from the system to launch their own brands or obtain other brands.

(177) Buying power may increase the risk of collusion between buyers. Thus, it appreciably changes the analysis of the anti-competitive effects of selective distribution. Foreclosure of more efficient retailers will especially arise in those cases where a strong organization of buyers imposes selection criteria on the supplier aimed at limiting distribution to the advantage of its members.

(178) In accordance with article 5.1(c) of the Communiqué, the supplier may not impose obligations to prevent the sales of those brands produced by certain competitors, either directly or indirectly. This condition aims specifically at avoiding

horizontal collusion to exclude particular brands by the leading suppliers through the use of selective distribution agreements.

(179) Foreclosure of other suppliers is normally not a problem as long as other suppliers can use the same distributors, that is, as long as the selective distribution system is not combined with single branding. In the case of markets with a dense network of authorized distributors or in the case of a cumulative effect, the combination of selective distribution and a non-competition obligation may lead to the foreclosure of competing suppliers. In that case, the principles set out in these Guidelines with relation to single branding agreements shall be applicable. Even if selective distribution is not combined with a non-competition obligation, foreclosure of suppliers may still be a problem if the leading suppliers apply not only purely qualitative selection criteria, but impose on their sellers certain additional restrictions, such as the obligation to achieve a minimum sales ratio or to reserve a minimum shelf-space. Such a problem is unlikely to arise if the market coverage by selective distribution is below 50% or, where this ratio is exceeded, if the aggregate market share of the five largest suppliers is below 50%.

(180) Maturity of the market is important in the assessment of selective distribution systems, as well. The loss of intra-brand competition and the risk of foreclosure of suppliers or distributors may be a serious risk in mature markets, but this is less likely in markets with growing demand, changing technologies and changing market positions.

(181) Selective distribution may lead to efficiencies when it allows savings in logistical costs due to economies of scale, irrespective of the nature of the product. However, this is a marginal efficiency in selective distribution systems. The nature of the product is very important to help solve a free-rider problem between the distributors or to help create a brand image, . In general, the case is strongest for new products, complex products, products whose qualities are difficult to judge before consumption and whose qualities are difficult to judge even after consumption. The combination of selective distribution with exclusive distribution may create competition problems within the framework of article 4 of the Act, if the market share of the implementing supplier is above 40% or in case of cumulative effects, even where active sales between regions are not restricted. As an exception, such a combination may fulfill the conditions of exemption if it is necessary for the protection of fundamental and relationship-specific investments made by the authorized sellers.

(182) To ensure that the least anti-competitive restraint is chosen, it is relevant to see whether the same efficiencies can be obtained at a comparable cost by for instance introducing service requirements alone.

Example of Quantitative Selective Distribution

(183) Brand A, which is the market leader for a particular consumer durable, sells its product through a selective distribution network. A's market share is 45%. There are several criteria for admission to the selective distribution network. The store must employ trained staff and provide pre-sales services. In addition, there must be an area in the store devoted to the sales of the product and similar hi-tech products, the store must sell a wide range of the products of the supplier, and the products must be displayed in an attractive manner. Moreover, the number of admissible retailers in the

network is limited through the establishment of a maximum number of retailers depending on the population of each province. Producer A has six competitors with its three largest competitors, B, C and D, having market shares of respectively 20%, 15% and 10%. A is the only manufacturer to use selective distribution and the distributors of A also handle a some competing brands. In addition, competing brands are also widely sold by other distributors which are not a member of A's selective distribution network. Brands B and C are sold in most of A's selective distribution network, but also in other sellers providing a high quality service and in hypermarkets. Brand D is mainly sold in sellers with high quality service. Technology is evolving quite rapidly in this market, and the main suppliers have established a strong image for their products through advertising.

(184) In this market, the coverage ratio of selective distribution is 45% and this system does not affect inter-brand competition directly. Intra-brand competition may be reduced due to the selective distribution system of brand A, but consumers have access to similar quality brands B and C, with a combination of low service and low prices. There is no limitation on the distributors in the selective distribution system to sell competing brands, and the limitation on the number of distributors that can sell A leaves other high service distributors free to distribute competing brands. Therefore, there are no concerns of foreclosure effects for other brands. Since the selective distribution system of A has a limited restrictive effect on intra-brand competition due to the aforementioned reasons, it is likely for the system in question to meet the exemption conditions.

Example of Selective Distribution with Cumulative Effect

(185) In a market for a particular sports article, there are seven manufacturers, with market shares of 25%, 20%, 15%, 15%, 10%, 8% and 7%. The five largest manufacturers distribute their products through quantitative selective distribution, whilst the other two use different distribution systems. As a result, selective distribution covers 85% of the market. The criteria for access to the selective distribution networks are mostly uniform amongst manufacturers. The stores are required to have qualified personnel and to provide pre-sale services. There must be an area in the store devoted to the sales of these goods (a specialty area) and a minimum size for this area is specified. The store is required to sell a wide range of the relevant products and to display the article in an attractive manner. The store must be located in a commercial street, and that type of goods must represent at least 30% of the total turnover of the store. In general, the same seller is a member of the selective distribution system for all five manufacturers. The two brands which do not use selective distribution usually sell through less specialized retailers with lower service levels. The market is stable, both on the supply and on the demand side, and there is strong brand image and product differentiation. The five market leaders have strong brand images, acquired through advertising and sponsoring. On the other hand, the other two manufacturers have a strategy of cheaper products, with no strong brand image.

(186) In this market, access by general price discounters to the distribution networks of the five leading producers is denied. Indeed, the requirement that this type of goods represents at least 30% of the total sales and the criterion on pre-sales services rule out most price discounters from the network of authorized dealers. As a consequence, consumer choice is restricted, since they are required to buy one of the five leading brands from stores providing higher quality and more expensive services. This

situation leads to reduced inter-brand competition between the five leading brands. The fact that the two smallest brands can be bought in low service/low price shops does not compensate for this, because the brand image of these five brands is much better. Inter-brand competition is also limited through multiple dealership. Even though there exists some degree of intra-brand competition and the number of retailers is not directly limited, the criteria for admission to the selective distribution network are strict enough to lead to a small number of retailers for the five leading brands in each region.

(187) The efficiencies associated with these quantitative selective distribution systems are low: Since the product is not very complex, it does not justify a particularly high service. Unless the producers can demonstrate clear efficiencies arising from their networks of selective distribution, the block exemption may have to be withdrawn because of its cumulative effects resulting in less choice and higher prices for consumers.

9.5.2.5. Franchise Agreements

(188) Franchise agreements contain licenses of intellectual property rights and know-how relating in particular to trade marks, signs, etc. for the distribution of goods or services. In addition to the license of intellectual IPRs and know-how, the franchisor usually provides the franchisee during the life of the agreement with commercial or technical assistance. The license and the assistance are integral components of the business method within the franchise package. The franchisor is in general paid a franchise fee by the franchisee for these elements. Franchising enables the franchisor to establish, with limited investments, a uniform distribution network for its products. In addition to the provisions on the business method, franchise agreements usually contain a combination of different vertical restrictions concerning the products being distributed, in particular selective distribution and/or non-competition and/or exclusive distribution or weaker forms thereof.

(189) The principles related to the coverage by the Communiqué of the franchise agreements granting IPR and know-how licenses are dealt with in the relevant sections of the Guidelines. As for the vertical restraints on the purchase, sale and resale of goods and services within a franchising arrangement, such as selective distribution, non-competition obligations or exclusive distribution, the Communiqué applies up to the 40% market share threshold for the franchisor or for suppliers appointed by the franchisor. The previous guidance provided in respect of those types of restrictions applies also to franchise agreements, subject to the following remarks:

(i) The more important the transfer of know-how, the easier it is for the vertical restrictions to meet the exemption criteria.

(ii) A non-competition obligation concerning the goods or services purchased by the franchisee falls outside the scope of article 4 of the Act where such an obligation is necessary to maintain the common identity and prestige of the franchised network. In such cases, the duration of the non-competition obligation will not cause a problem under article 4 either, as long as it does not exceed the duration of the franchise agreement itself.

Example of Franchise Agreement

(190) A manufacturer has developed a new format for selling sweets in so-called fun shops where the sweets can be colored on demand from the consumer. The manufacturer of the sweets has also developed the machines to color the sweets. The manufacturer also produces the coloring liquids. The quality and freshness of the liquid is of vital importance to producing sweets. The manufacturer made a success in the sale of its sweets through a number of own retail outlets all operating under the same trade name and with the uniform fun image (style of the shops, common advertising etc.). In order to expand sales the manufacturer started a franchising system. The franchisees are obliged to buy the sweets, liquid and coloring machine from the franchisor, to operate under the same trade name and image, pay a franchise fee, contribute to common advertising costs and ensure the confidentiality of the business concerning the operation provided by the franchisor. In addition, the franchisees are only allowed to sell out of the building (premises) assigned to them, only to final consumers or other franchisees; they are not allowed to sell other sweets. The franchisor will not appoint another franchisee nor operate a retail outlet itself in a given contract region. The franchisor is also under the obligation to develop its products, its business outlook and the system of operation and make these available to all retail franchisees. The franchise agreements are concluded for a duration of 10 years.

(191) Sweet retailers have to buy their sweets from either national producers or from importer wholesalers who also sell products from national producers. In this market, the franchisor's sweets compete with other brands of sweets. The franchisor has a market share of 45% in the retail market for sweets. Competition is between national and international brands, some of which produce a wide range of foodstuff. There are many potential outlets for sweets in the form of tobacconists, general food retailers, cafeterias and specialized sweet shops. The franchisor's market share in the market for machines for coloring food is 10%.

(192) Most of the obligations contained in the franchise agreements can be deemed necessary to protect intellectual property rights or maintain the common identity and product of the franchised network, therefore they may be said to fall outside the scope of article 4 of the Act. The restrictions on selling (contract region, selective distribution) provide an incentive to the franchisees to invest in the coloring machines and the franchise system and, if it's not necessary, it at least helps maintain the common identity, thereby offsetting the loss of intra-brand competition. The non-competition clause for the full duration of the agreement allows the franchisor to keep the outlets uniform and prevent competitors from benefiting from its trade name. It does not lead to a foreclosure effect, as long as other sweet producers do not encounter difficulties in finding a great number of potential outlets. Such a franchise agreements is likely to benefit from the exemption within the framework of article 5 of the Act.

9.5.2.6. Exclusive Supply

(193) Article 3.1(h) of the Communiqué defines exclusive supply obligation as a direct or indirect obligation on the supplier to sell the contract goods or services only to a single buyer within the national borders for its own use or for resale. The subparagraph in question specifies an exceptional distribution restraint. In accordance with the agreement, the supplier sells a certain final product to a single buyer within the national borders. For intermediate goods and services, exclusive supply indicates

that there is a single buyer within Turkey or that there is a single buyer within Turkey that uses these goods for a specific purpose. For intermediate goods and services, exclusive supply is generally known as industrial supply.

(194) Vertical agreements containing exclusive supply obligations in accordance with article 3.1(h) of the Communiqué can benefit from the block exemption, provided the buyer's market share does not exceed 40% in accordance with article 2.3 of the Communiqué and the conditions of specified in this Communiqué are fulfilled. The following explanations can provide guidance for the undertakings where the market share thresholds are exceeded.

(195) The main competition risk of exclusive supply is anticompetitive foreclosure of other buyers. The market share in the upstream purchase market is obviously important for assessing the ability of the buyer to impose exclusive supply obligations which foreclose other buyers from access to supplies. The importance of the buyer on the downstream market is however an important factor in determining whether a competition problem may arise. If the buyer has no market power downstream, then no appreciable negative effects for consumers can be expected. On the other hand, such negative effects may be expected when the market share of the buyer in the downstream market as well as the upstream purchase market exceeds 40%. Even if the market share of the buyer in the upstream market does not exceed 40%, significant foreclosure effects may still result, especially when the market share of the buyer in the downstream market is over 40%. In this case the exemption may have to be withdrawn as well. If an undertaking is dominant in the downstream market, an obligation to sell only or mainly to the dominant buyer may easily result in anti-competitive effects.

(196) In the assessment of exclusive supply obligations, it is not only the market position of the buyer in the upstream and downstream markets that is important, but also the scope and duration of this obligation. The higher the tied supply share, and the longer the duration of the exclusive supply, the more likely it is to encounter foreclosure effects. Exclusive supply agreements concluded by a non-dominant undertaking for a period of less than five years require a balancing of pro- and anti-competitive effects. For agreements lasting longer than five years, most types of investments are not necessary to achieve the claimed efficiencies or the efficiencies are insufficient to outweigh the foreclosure effects of such exclusive supply agreements.

(197) The market position of the competing buyers in the upstream market is also important. This is because if competing buyers are significantly smaller than the foreclosing buyer, it is likely that they will be foreclosed for anti-competitive reasons, such as increasing costs. Foreclosure of competing buyers will not be a concern where those competitors have similar buying power and can offer the suppliers similar sales possibilities. In such a case, foreclosure could only occur for potential entrants. To wit, foreclosure effects may arise if all of the major buyers in a market enter into such agreements with the majority of suppliers. Such a cumulative effect may lead to withdrawal of the exclusivity.

(198) Entry barriers at the supplier level are important in establishing whether there is real foreclosure. In as far as it is efficient for competing buyers to provide the goods or

services themselves via upstream vertical integration, foreclosure is unlikely to cause competitive problems. However, in practice, there are often significant entry barriers.

(199) Countervailing power of suppliers is important. This is because large suppliers will not easily allow themselves to be cut off from alternative buyers. Foreclosure is therefore mainly a risk in the case of weak suppliers and strong buyers. In the case of strong suppliers, the exclusive supply obligations may be found in combination with non-competition obligations. The combination with non-competition obligations requires the application of the single branding rules of the Guidelines. Where both sides make relationship-specific investments, the combination of both types of restrictions, such as industrial supply agreements with mutual exclusivity, may often be justified below the level of dominance.

(200) Lastly, the level of trade and the nature of the product are important factors for foreclosure. Anticompetitive foreclosure is less likely in the case of intermediate products or where the product is homogeneous. Firstly, a foreclosed manufacturer that uses a certain input usually has more flexibility to respond to the demand of its customers than the wholesaler or retailer when compared to the demand by final consumers where brand plays an important role. Secondly, the loss of a possible source of supply matters less for the foreclosed buyers in the case of homogeneous products than in the case of a heterogeneous product with different grades and qualities.

(201) Below the level of dominant position, competition restriction in agreements are likely to get exemption in relation to homogenous intermediate goods. For final branded products or differentiated intermediate products where there are entry barriers, exclusive supply may have adverse effects on competition where the competing buyers are relatively small compared to the foreclosing buyer, even if the latter is not dominant in the downstream market.

(202) If anti-competitive effects are identified, exemption is still possible if the undertaking is not dominant. Efficiencies can be expected in the case of a hold-up problem, and such efficiencies are more likely for intermediate products than for final products. Other efficiencies are less likely. The presence of possible economies of scale in distribution do not seem likely to justify exclusive supply.

(203) In the case of a hold-up problem and even more so in the case of economies of scale in distribution, quantity forcing on the supplier, such as minimum supply requirements, could be a less restrictive alternative.

Example of Exclusive Supply Obligations

(204) In a market for a certain type of components (intermediate product market) supplier A agrees with buyer B to develop, with its own know-how and considerable investment in new machines and with the help of specifications supplied by buyer B, a different version of the component.

(205) B has to make considerable investments to incorporate the new component. A will supply the new product only to buyer B for a period of five years from the date of first entry on the market. B is obliged to buy the new product only from A for the same period. Both A and B can continue to sell and buy other versions of the component

elsewhere. The market share of buyer B in the upstream component market and on the downstream final goods market is a little over 45%. The market share of the component supplier is 35%. There are two other suppliers with around 20-25% market share and a number of small suppliers in the component market.

(206) Given the considerable investments, the agreement is likely to fulfil the conditions of exemption, due to the efficiencies created and the limited foreclosure effect. Other buyers are foreclosed from a particular version of a product of a supplier with 35% market share. However, there are other component suppliers in the market that could develop similar new products. The foreclosure of buyer B's demand to other suppliers (producers) is limited to maximum 45% of the market.

(207) Exclusive supply obligations require the supplier to sell to a single buyer, either directly or indirectly. Quantity forcing on the supplier, on the other hand, is based on incentives agreed upon by the buyer and supplier in order to ensure that the sales of the supplier are focused on the buyer. Within this framework, quantity forcing on the supplier can have effects similar to but weaker than exclusive supply obligations. In assessing the quantity forcing, the degree of foreclosure of other buyers in the upstream market is taken into consideration.

9.5.2.7. Tying

(208) Tying refers to situations where the supplier requires that to purchase one product, another distinct product should be purchased from the same supplier or someone designated by the latter. The first product is the tying product, and the second is the tied product. Tying obligations may constitute an abuse within the meaning of article 6 of the Act no 4054 in case of dominance. Article 4 of the Act no 4054 is applied to horizontal agreements where the sale of a product is tied to the purchase of a distinct one between competing undertakings. Tying may also constitute a vertical restriction under article 4 of the Act if it results in a single branding type of obligation for the tied product. Only the latter situation is dealt with in these Guidelines.

(209) Whether products will be considered as distinct depends primarily on customer demand. Two products in question are distinct where, in the absence of the tying, the customers can buy the products from two separate markets. For instance, since customers will want to buy shoes with laces, it has become commercial usage for shoe manufacturers to supply shoes with laces. Therefore, the sale of shoes with laces is not a tying practice. Where the nature of the product makes it technically difficult to sell one product without the other, this practice becomes acceptable.

(210) The main negative effect of tying on competition is the risk of market foreclosure for the tied product. Tying means that there is at least a quantity-forcing obligation on the buyer in respect of the tied product. Where in addition a non-competition obligation is introduced in respect of the tied product, the possible foreclosure effects in the tied product market will increase. Tying may also lead to prices that are above the competitive level, especially in three situations. The first of these is where the tying and the tied product are partial substitutes for the buyer. The second is where tying allows price discrimination with respect to the customer using the product, for example the tying of ink cartridges to the sale of photocopying machines. Thirdly, in long-term agreements or in after-sales markets for original equipment with long replacement periods, it becomes difficult for customers to calculate the outcomes of the tying.

Finally, tying can also lead to an increase in entry barriers, both in the tied and the tying product markets.

(211) Vertical agreements containing tying obligations can benefit from the block exemption where, in accordance with article 2.2 of the Communiqué, the market share of the supplier does not exceed the 40% threshold both for the tied and the tying product, provided that it fulfills the conditions specified in the Communiqué. Tying may be combined with other vertical restraints that are not prohibited under that Regulation, such as non-competition obligations or quantity forcing in respect of the tying product, or exclusive sourcing. The following explanations may provide guidance for undertakings in those individual cases where market share threshold is exceeded.

(212) The market position of the supplier in the market of the tying product is of central importance to assess possible anti-competitive effects. In general, this type of agreement is imposed by the supplier. The importance of the supplier in the tying product market is the main reason why a buyer may find it difficult to refuse a tying obligation.

(213) The market position of the supplier's competitors in the tying product market is important in assessing the supplier's market power. As long as competitors are sufficiently numerous and relatively strong, no anti-competitive effects can be expected, as buyers will have sufficient alternatives to purchase the tying product without the tied product, unless other suppliers are applying similar obligations. In addition, entry barriers in the market of the tying product are important in establishing the market power of the supplier. When tying is combined with a non-competition obligation in respect of the tying product, this considerably strengthens the position of the supplier.

(214) Buying power is relevant, as important buyers will not easily be forced to accept tying without obtaining at least part of the possible efficiency increases. Tying not based on efficiency is therefore mainly a risk where buyers do not have significant buying power.

(215) Where anti-competitive effects are established, the question whether exemption is possible according to article 5 arises as long as the undertaking does not hold dominant position. Tying obligations help to produce efficiencies in joint production and joint distribution. Where the tied product is not produced by the supplier, an efficiency may also arise since the supplier will buy large quantities of the tied product. For tying to be granted exemption, however, it must be shown that at least part of the cost reductions are passed on to the consumer. If the retailer is able to obtain, on a regular basis, the products offered by the supplier applying the tying practice or similar products on the same or better conditions, then the exemption will not be granted.

(216) Another efficiency increase may exist where tying helps to ensure a certain uniformity and quality standards. However, it needs to be demonstrated that these positive effects cannot be realized equally efficiently by requiring the buyer to use or resell products satisfying minimum quality standards, without requiring the buyer to purchase these from the supplier or someone designated by the latter. The requirements concerning minimum quality standards would not normally fall within the scope of article 4 of the Act. Where the supplier of the tying product imposes on the buyer an obligation concerning the suppliers from which the buyer must purchase the

tied product, for instance because the formulation of minimum quality standards is not possible, this may also fall outside the scope of article 4, especially if the supplier of the tying product does not derive a direct (financial) benefit from designating the supplier of the tied product.

(217) If tying results in prices which are above the competitive level, this in itself will be considered to be anti-competitive. The foreclosure effect depends on the tied percentage of total sales in the market of the tied product. On the question of to what extent this effect will lead to an appreciable foreclosure effect in the market, the assessment for single branding can be applied here as well. Exemption above the 40% threshold is not possible as long as there are no efficiencies at least partially passed on to the consumer. When tying is combined with non-competition obligations with respect to the tying or tied product, the likelihood of exemption is even lower.

(218) If there are no efficiencies as a result of the tying agreement or if the efficiencies created are not passed on to the consumer, the block exemption may be withdrawn. The exemption may also be withdrawn in cases of cumulative effect where most suppliers enter into similar tying agreements and any possible efficiencies are not, even partially, passed on to the consumers.

9.5.2.8. Recommended Prices and Maximum Sales Price Maintenance

(219) Where the supplier's market share does not exceed 40%, recommended price and maximum price practices are evaluated within the scope of the block exemption, as mentioned in the relevant chapters. The following explanations will provide guidance in the assessment of individual cases where the market share threshold is exceeded and where the block exemption must be withdrawn.

(220) Possible competition risks in maximum or recommended prices arise primarily where maximum and recommended prices function as a reference for resellers, most or all of whom comply with those prices. Secondly, recommended and maximum prices facilitate collusion amongst suppliers.

(221) The most important factor in the assessment of possible anti-competitive effects of maximum or recommended prices is the market position of the supplier. The stronger the position of the supplier, the higher the risk of maximum or recommended prices being used somewhat uniformly by resellers, since they may use these prices as a focal point. Resellers may find it hard to deviate from the price recommended by such an important supplier. Under these circumstances, if maximum and recommended prices result in uniformity of price levels, these practices are not likely to fulfill the conditions of article 5 of the Act.

(222) The second important factor for the assessment of possible anti-competitive effects of maximum or recommended prices is the position of the competitors within the market. Especially in tight oligopolistic markets, publication and use of maximum or recommended prices may facilitate collusion amongst suppliers, by enhancing price transparency at the chosen price level and by reducing the likelihood of lower prices in the market. Maximum or recommended prices which result in such effects may violate article 4 of the Act.

9.5.2.9. Most Favored Customer Clause

(223) The use of the most favored customer (MFC) clauses does not always result in the same competitive consequences in the market. Although this clause may have positive effects on competition in the market, it may also lead to some negative competitive effects. Consequently, in competition law assessments involving MFC clauses, the market positions of the party benefiting from the clause as well as its competitors, the goal of including the clause in the agreement, and the self-characteristics of the market and the clause must be examined in detail. Nonetheless, an agreement with an MFC clause may, in principle, benefit from the block exemption provided the market share of the party in favor of which the clause is implemented¹⁰ does not exceed 40% and the other conditions listed in the Communiqué are fulfilled. Where the market share threshold is exceeded, the following examples may be instructive for individual assessment.

(224) For example, retroactive MFC clauses¹¹, which allow the favored buyer to receive more advantageous offers under all circumstances or which additionally increase the cost for the supplier to offer discounts to those buyers which are not parties to the clause can generally harm competition more than other clauses. In addition, it may be said that MFC clauses cause more harm to competition where the parties to such clauses (especially the party in whose favor the clause is implemented) hold market power in comparison to their competitors in the market. Under such circumstances, these conditions may exclude those competitors who are not parties to the agreement and foreclose the market to competing undertakings. Also, the use of such conditions in concentrated markets are more concerning than their use in non-concentrated markets. This is because, in concentrated markets, competing buyers who are not parties to these clauses are less likely to find alternative suppliers. Additionally, a more skeptical approach needs to be adopted in assessing MFC clauses where the use of these clauses in the market proliferates and thus a large portion of the market becomes subject to such conditions. This is due to the fact that widespread use of these conditions in the market would increase the likelihood of a cumulative increase in the anti-competitive effects caused by the clauses, thereby restricting competition.

(225) On the other hand, sometimes the use of MFC clauses may not lead to any competitive concerns. For example, where both parties to an agreement with this clause lack market power, the use of such clauses are less likely to cause competitive concerns. When used by small buyers with no market power, it may be said that MFC clauses allow these buyers to benefit from affordable prices and conditions in the market and thus have positive effects on competition in the market. Where the level of concentration in the upstream market is low, i.e. where the upstream market is sufficiently competitive, competitive harm may not occur since existing and potential

¹⁰ MFC clauses may be assessed differently in conventional markets and in markets with online platforms. For instance, in conventional markets, the party in favor of which this clause is implemented is the buyer, while in markets with online platforms, the party in favor of which this clause is implemented may be the supplier, buyer or mediator, depending on the relevant product market. Consequently, the Communiqué no 2002/2 does not specify which party's market share will serve as the basis, instead states that the market share of the party in favor of which the clause is implemented in the agreement shall be taken as the basis in the calculation.

¹¹ Retroactive MFC clause: Used to refer to those circumstances where the relevant buyer is paid the difference between the lower prices offered to those buyers who were not parties to the MFC clauses in the past and the prices offered to the buyer who is a party to the MFC clause.

rivals may choose other alternatives. Also, MFC clauses will have relatively smaller negative effects on competition in non-transparent markets, since the implementation of the MFC clauses in the market cannot be efficiently monitored.

9.5.2.10. Other Vertical Restrictions

(226) Vertical restrictions listed above and their combinations are intended only as examples. There may be other restrictions and combinations thereof, which are not specifically explained within these Guidelines. The same general principles will apply to such restrictions and combinations of restrictions, with particular attention given to the effects on the market.