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Possible discrimination between members of two different networks: how to avoid possible problems

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Outline

1. Overview of the distribution strategies and marketing practices
1. The concept of discrimination
1. Discrimination and legal theory of harm
4. Conclusions



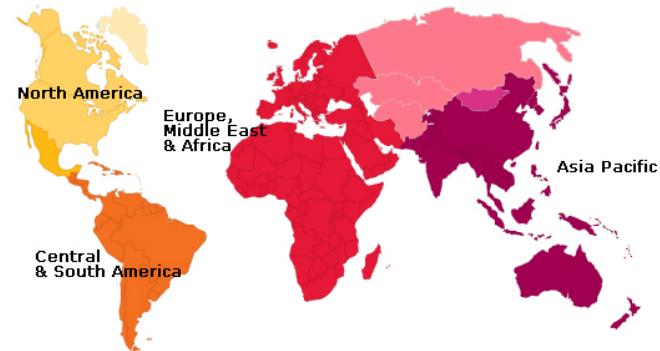
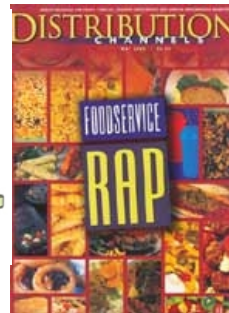
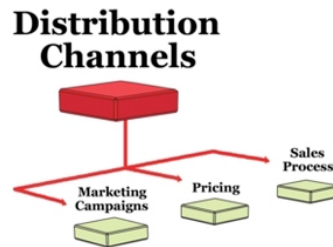
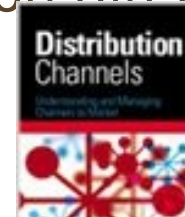
1. Overview of the distributions strategies and marketing practices by territory

Distribution strategies are different among the Gucci regions: they are consistent with the regions typical market uses

USA: Gucci America: DOS + spread out distribution through Dep.Stores .

ASIA: no multibrand in Asia, whereby only DOS, Franchisee or

Duty free JAPAN: only DOS or concession directly owned in Dept.Stores



Overview of distribution strategies by channels

- Distribution Channels:
 - Retail
 - a- Mono brand boutique
 - b- Flagship store
 - c- Franchising
 - Wholesale
 - a- Dept. Store
 - b- Multi-brand boutique
 - Other Channels
 - a- Internet
 - b- Duty-free shops

Gucci distribution networks (vs Chanel, Hermes)

Gucci currently adopts several methods of distribution and certainly incurs in **dual distribution (we produce, we supply and we sell)**: not only we have the same products offered at both the retail and “classic” wholesale level

- Directly owned stores (DOS);
- Franchisees;
- Multibrands;
- Selected Corners in Department Stores – Duty Free shops but we also have the same products offered through different additional channels:
- Outlets;
- Internet: “*Gucci.com*” – “*net a porter*”



Gucci in the world

330+ directly owned stores

35+ stores in franchising worldwide

500+ multibrands stores offering Gucci products in Europe

Approximately 40 contracts for wholesale distribution of watches

4 agents to promote Gucci watches in Italy



Why DOS



Why DOS

PRO'S

- Margins & revenues – from industrial cost to sale price
- Direct management of the luxury image
- Presence in extra luxury environment – no limit to expansion – no exclusivity restrictions: 2-3 stores in the same town
- Flag ship stores that allow a full experience in the Gucci world
- Personalized Treatment of the clientele: Made to Order and Embossing Program; Personalized orders (VIP); VIP events (Gucci Master), CRM cards
- Unique initiatives: Fiat, Riva, Bianchi
- Special editions of products – only for DOS
- Constant upgrade and renovation in style (Frida I)
- Unique experience: The Artisan Corner
- Celebration of the 90° anniversary – opening of Gucci Museum

CON'S

- Costs and expenditure; trained personell, inventory; strict guidelines



Equestrian



Gucci Limited edition for N Y opening

1921 collection



Artisan corner



500 by GUCCI

DOS or Franchising?



Why franchising

PRO'S

- For Franchisor:
 - direct penetration of the market, in strategic city/street, assured partnership which grants presence for five years;
 - for Franchisor almost no cost of investment (limited to dedicated structure to share among the many franchisees, guidelines and assistance, knowhow);
 - uniformity of consumer perception: perfect recognition by consumer of Gucci activity although through third party franchisee: same level of service, choice of products; same initiatives (Unicef);
 - strict control on stores constructions, purchases, daily activity, thorough reporting,
- For Franchisee:
 - benefiting of the Gucci world of each novelty in Gucci products and Gucci fame
- **CON 'S**
 - Responsibilities on franchisor (disclosure)
 - Contractual obligations on franchisee
 - Critical termination by substitution or by direct participation (JV)

M ultibrand !!!



Why multi brands

PRO's

- Very dynamic environment:
“must be” stores: it is strategic to be present in certain stores/areas
- Very flexible relationship:
in and out seasonally – no contract only gcs
- Very limited investement for the dealer and for Gucci
- Very limeted assistance from Gucci
- Very good channel for sales



CON'S

- No control on resale
- Weak control on image and pr activities



ALEXANDER WANG
AQUILANO E RIMONDI
BALENCIAGA BALMAIN
BOTTEGA VENETA BURBERRY
CAR SHOES CELINE CHLOÉ
CHRISTIAN DIOR
DOLCE & GABBANA DSQUARED2
FENDI GIAMBATTISTA VALLI
GUCCI JIMMY CHOO LANVIN
MAISON MARTIN MARGIELA
MARC JACOBS MISSONI
MIU MIU MONCLER
PIERRE HARDY PRADA
RICK OWENS
ROBERTO CAVALLI
ROGER VIVIER VALENTINO
VIONNET YVES SAINT LAURENT
GIUSEPPE ZANOTTI

Best distribution strategy for luxury goods?

	PROs	CONs
DOSs	<ul style="list-style-type: none"> ✓ direct management of the luxury image ✓ limited edition products (special for DOSs) ✓ unique initiatives (e.g. Fiat, Riva, Bianchi) <div>   </div>	<ul style="list-style-type: none"> ✓ cost & expenses ✓ trained personnel ✓ strict guidelines
Franchising	<ul style="list-style-type: none"> ✓ for the <i>franchisor</i>: direct penetration of the market; almost no investment costs; strict control on stores construction, purchases, daily activity etc. through reporting ✓ for the <i>franchisee</i>: benefiting of the Gucci fame for any new initiative 	<ul style="list-style-type: none"> ✓ responsabilization (disclosure) ✓ critical termination by substitution or by direct participation (JV)
Multi-brand stores	<ul style="list-style-type: none"> ✓ flexible relationship: in & out seasonally ✓ limited assistance from Gucci ✓ limited investments for the dealer and Gucci ✓ very good channel for sales 	<ul style="list-style-type: none"> ✓ No control on resale ✓ Weak control on image and PR activities

Other distribution networks: Direct Owned Outlets

PROs

- Discontinued merchandise into safe channel
- Continued sales margin
- Maintenance of the image and no mix-up with other brands
- Attraction of soft portfolio clients to be fidelized
- Presence in certain remoted areas, far from high street distribution
- Flexibility on prices: weekly offers, discounts
- Attracting other brands by managing outlet centre (mcarthur glenn system)



CONs

- Risk to fidelize outlets' clients only (such as internet clients)
- Reduced luxury experience if compared wit

2. The concept of discrimination



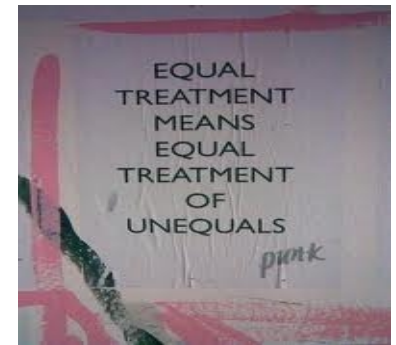
What is discrimination? How do I measure it?



Discrimination means *unequal treatment* in situations which are *identical*



Is it right?

The different treatment of non-comparable situations *does not* lead to discrimination



Not all differences in treatment are discriminatory: there may be situations in which different treatment may be justified - advantaging a type of dealer among different channels or one single dealer among the same type is not discrimination

Different networks= different treatment= discrimination?

	DOS and franchisees	Multibrand
<i>Prices</i>	Payment of royalties and advertising fees to the franchisor in exchange of exclusivity, know-how and assistance	No financial obligation besides merchandise payment
<i>Investment</i>	DOS, franchisees and some selected corners, are obliged to invest in the building up of the store, and in its maintenance (e.g. monthly windows)	
<i>Delivery</i>	Early delivery 	Slightly delayed 
<i>Assistance</i>	Common dedicated training for DOS and franchisees	Only printed material
<i>Buy back</i>	Buy back for DOS is guaranteed thanks to the Gucci owned outlets network; For franchisees, buy back only at expiration	For multibrands and corners no merchandise buy back

Critical issues arising from different distribution networks

- ✓ **Issues related to the co-existence of several distribution networks:**

- Sometimes DOS and multibrands do not necessarily get well along, although synergies and cross-selling are desired outcomes
- Sometimes multibrands and selected department stores may have a quite aggressive discount price policy (i.e. anticipated discount policy for privileged clients, but also DOS do it)

- ✓ **Issues concerning different price list and assortment**

- Franchisee do benefit of different price list and assortment

- ✓ **Issues concerning the return policy:**

- Homogeneous and advantageous return policy terms are offered for DOS and franchisees, *NOT* for multibrands and third party corners

- ✓ **Issues concerning the contract : yes (franchisee) no (multibrand)**

- ✓ **Call option: yes (franchisee) no (multibrand)**

- ✓ **Termination:**

- Paradoxically, there are more risks in termination of non-regulated multibrands than in regulated franchising agreements

Discrimination: in channels that are so different, discrimination should be really weighted: franchisee have lower price list, but have a call option at the end and tons of duty and obligations in the contract (roy, advertising, trademark protection, call option):

Legal issues arising from dual distribution

Dual distribution could turn a supplier and a retailer of the same brand into competitors in the retailer's market: the supplier competes with the dealer of its network, thus creating competition with itself.

This may lead to antitrust concerns as well as to legal issues concerning a possible discrimination.

As far as discrimination is concerned, we have to distinguish between:

- *The relationship between different competing distributors served by the same supplier:* in principle, discrimination is very unlikely because supplier has no interest to benefit one distributor or the other;
- *The relationship between supplier and dealers within dual distribution:* a supplier's conduct aimed at *benefiting its own stores versus third party dealers in the same network*, eg. withholding deliveries and assortment, might lead to the risk of discrimination.

3. Discrimination and legal theory of harm



Is discrimination a general obligation by law?

- Non discrimination is not a general principle : there is not an absolute veto to discriminate
- Discrimination is recalled in the cases of abuses or in the cases of unlawful antitrust conduct, breach of contract
- The real discrimination only arise if the identical situation are treated differently: but 90% of the different treatments are not really discriminatory they just derive from different practical situation, the right to contractually derogate is in the disposition of the parties


Discrimination among/within the various distribution channels



“Is there any obligation providing for equal treatment among the various distribution channels?”

National legislation usually provides for several obligations concerning, *inter alia*, the relationship between franchisor and franchisee, or consumer protection, but **what about equal treatment?**

Examples of non discrimination from national legislations



- In Italy, Law 129 of 2004 on franchising does not explicitly address the issue: it only imposes on the franchisor obligations of good faith and disclosure (art. 6): treat all the same way if there are the same starting conditions.

- art. 9 of Law 192 of 1998 on abuse of economic dependence prohibits such abuse, which also includes imposing on discriminatory contractual conditions: does it apply to distribution agreements? In principle NO, as it only deals with supply contracts (limited scope of application) where the supplier is under economic dependence – Gucci products are indispensable-

BUT

the law can be applied by analogy to all relationship in which there is economic dependence – but it must be demonstrated if a retailer or a franchisee is such conditions, that are weak party, otherwise any different treatment even discriminatory cannot be sanctioned

Examples of non discrimination from national legislations

In France: no codified mention of franchise agreements in French law, there are no specific legal provisions applicable to franchises. General contractual aspects are governed by the Civil Code (e.g. general principle of good faith in contractual relationships, art. 1134) and commercial aspects are governed by the Commercial Code: art. L 420-2 on *exploitation abusive de l'état de dépendance économique* (abuse of economic dependence), which reads:

« Ces abus peuvent notamment consister en ... pratiques discriminatoires »

BUT see French Competition Authority: that provision is not applicable to a retailer that, although having a privileged relationship with a brand, can still diversify its supplying sources (Decision 01-D-49 of 31 August 2001, confirmed in appeal). As Retailer cannot demonstrate economic dependence

Examples of non discrimination from the EU



Discrimination cases are frequent in **abuse of dominance** cases. Art. 102 of the TFUE gives a specific example of abuse, consisting in

“applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage”

In that case, the legal test implies, first, the existence of a dominant position in the relevant market and, second, it has to be considered what constitutes an abuse.

BUT

an *objective justification* may constitute a defence, such as efficiencies (the discriminatory conduct could it be a more effective distribution system, reaching more end consumers and thus improving demand for products?).

Examples of non discrimination from the E U

As for **agreements**, ex art 101 TFUE, “apply dissimilar condition to equivalent transactions with other trading parties thereby placing them at competitive disadvantages” discrimination could be sanctioned: but in reality it is very unlikely to find agreements which are contrary to the EU competition rules.

Different situation is if discrimination is made to reach unlawful objectives: this has been sanctioned by antitrust authorities (price fixing, parallel market): here discrimination is a tool to reach an unlawful goal, it is not the goal itself!

Instead, the agreement should be assessed on the basis of the national (civil/contract law) provisions or under the terms of the distribution contract at issue.

E.g.: “*most favoured customer clause*”: discrimination may occur because the terms of the contract have been infringed by one of the parties, for instance when the supplier has not given the same discount he gives to the customer enjoying the clause.

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No obligation for equal treatment on different distribution channels, besides those imposed by law and those offered voluntarily by one of the parties: no duty to conclude a contract at the same conditions because each case is a different story



All the players within a distribution network work in a very competitive environment, and as third party multibrand stores are free to organize their sales, offers, website, so is Gucci free to offer different economic conditions/deliveries to its distribution channels. For those as franchisees who devote time and investment for Gucci, we reserve different conditions compared to those making very limited or zero investment. Practical examples include transfer price, delivery, PR initiatives (Unicef)

Discrimination within the same distribution channel?

Question much more tricky, but still very unlikely.

Example: within a franchising network:

renouncing to royalties, and/or to advertising contribution; offering economic support for start up period in different ways (different payments conditions among the stores)

here discrimination is certainly more evident and less acceptable by other franchisees



The ratio stays:

- in different initial investment costs that may justify, for example, capex contribution;
- the opening of a franchisee in certain sensitive areas may require the franchisor to compromise for the benefit of the franchisee;
- there are no legal constraints for companies to agree such contractual derogations: the company is free to compromise, to achieve its strategy to be present in certain areas.

Example: with reference to multibrands stores:

different payment conditions are normal practice because of different finance capability;

Example: with reference to corner and franchising:

for consumers' perception corners in selected department stores (e.g. Breuninger), and franchisees within multibrand stores (Ancona, Italy) - when a free-standing store is not appreciated - are the same; but the latter pays royalties and advertising fees;

Example: corner/duty free shops in airport and franchising:

for consumers' perception they are the same, but the one pays royalties and advertising fees, the other does not.

4. Conclusions

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"I didn't just jump to conclusions. I hopped
and skipped first."

Conclusions

Constructive or functional discrimination

does not amount to effective discrimination and is lawful provide that:

- Terms of the contract have not been infringed
- Principles of good faith (or other equivalent general principles of contract law) have not been infringed
- The terms of the contract and the parties' conduct comply with the relevant legislations no unlawful goal behind certain discriminatory conduct



- Art. 9.

- Abuso di dipendenza economica*

- 1. È vietato l'abuso da parte di una o più imprese dello stato di dipendenza economica nel quale si trova, nei suoi o nei loro riguardi, una impresa cliente o fornitrice. Si considera dipendenza economica la situazione in cui un'impresa sia in grado di determinare, nei rapporti commerciali con un'altra impresa, un eccessivo squilibrio di diritti e di obblighi. La dipendenza economica è valutata tenendo conto anche della reale possibilità per la parte che abbia subito l'abuso di reperire sul mercato alternative soddisfacenti.
 - 2. L'abuso può anche consistere nel rifiuto di vendere o nel rifiuto di comprare, nella imposizione di condizioni contrattuali ingiustificatamente gravose o discriminatorie, nella interruzione arbitraria delle relazioni commerciali in atto.
 - 3. Il patto attraverso il quale si realizzi l'abuso di dipendenza economica è nullo.

Articolo 101

(ex articolo 81 del TCE)

1. Sono incompatibili con il mercato interno e vietati tutti gli accordi tra imprese, tutte le decisioni

di associazioni di imprese e tutte le pratiche concordate che possano pregiudicare il commercio tra

Stati membri e che abbiano per oggetto o per effetto di impedire, restringere o falsare il gioco della

concorrenza all'interno del mercato interno ed in particolare quelli consistenti nel:

a) fissare direttamente o indirettamente i prezzi d'acquisto o di vendita ovvero altre condizioni di

transazione;

b) limitare o controllare la produzione, gli sbocchi, lo sviluppo tecnico o gli investimenti;

c) ripartire i mercati o le fonti di approvvigionamento;

d) applicare, nei rapporti commerciali con gli altri contraenti, condizioni dissimili per prestazioni

equivalenti, così da determinare per questi ultimi uno svantaggio nella concorrenza;

e) subordinare la conclusione di contratti all'accettazione da parte degli altri contraenti di prestazioni

supplementari, che, per loro natura o secondo gli usi commerciali, non abbiano alcun nesso con

l'oggetto dei contratti stessi.

2. Gli accordi o decisioni, vietati in virtù del presente articolo, sono nulli di pieno diritto.

