

Workshop Assonime- EUI RSCAS
Innovation and Market Power in the Food Supply Chain:
Challenges for Competition Policy and Regulation

**Food supply chain:
the role of competition policy and the new
rules on unfair trading practices**

Ginevra Bruzzone

Assonime and LUISS School of European Political Economy

Fiesole, 20 September 2019

Outline

Setting the scene

- Ongoing developments in the food supply chain
- The EU institutional framework: interplay of the different policy tools
- Objectives of competition policy versus CAP objectives

Three questions

- a. What can be achieved by means of the application of competition rules?
- b. Which boundaries for the regulation of fairness in B2B relationships?
- c. Which model for enforcement?

Setting the scene

Ongoing developments in the food supply chain

- ✓ impact of the digital transformation on business models (production and commercialization) => efficiency, sustainability, scope of relevant markets etc.
- ✓ global v. national v. local dimension
- ✓ concentration/consolidation at the different levels of the value chain => issues of market power and bargaining power; use of horizontal cooperation agreements as a tool to increase bargaining power
- ✓ New players/ platforms
- ✓ Vertical integration/ private labels

Markets along the supply chain are closely interrelated => public policy should consider the overall framework

Several policy tools in the EU institutional framework

Relevant policy areas include:

- Competition rules
- Common Agricultural Policy (CAP) – including exception to the application of competition rules (art. 42 TFEU)
- Consumer protection (safety, unfair commercial practices, etc.) (some Member States extend to micro/small enterprises)
- Digital Single Market Strategy: connectivity; trust in online transactions; cross border e-commerce; level playing field for traditional and new market players; supporting innovation and the ability of SMEs to exploit the potential of the digital transformation; skills and requalification of workforce
- Trade policy

The interplay of the different tools

- The choice of the proper mix of policies for the agricultural and food supply chain and the interplay of the different sets of rules are hotly debated issues. See for instance:
 - amendments to the CMO Regulation 1308/2013 by the Omnibus Regulation 2017/2393 (added during the legislative process)
 - different emphasis in Study requested by the Agri Committee of the EP on *New Competition Rules for the Agri-Food Chain in the CAP post 2020*, September 2018, versus Report by the European Commission on *The application of competition rules to the agricultural sector*, October 2018
- how should we combine the different policy measures in such a way as to minimize trade-offs and make the most of complementarities?

Focus on the interplay of competition law and rules on unfair trading practices

The objectives of competition policy versus CAP objectives

Goal of EU competition rules: protection of the competitive process as a means to ensure efficiency and to protect consumers

=> *boundaries of legitimate conduct*: agreements, unilateral conduct by dominant undertakings and mergers are prohibited, on the basis of a theory of harm, when expected to have a negative impact on competitive variables (price, quantity, variety, quality, innovation)

=> *assessment*: depending on whether the restriction is intrinsically harmful, by object approach or case by case impact assessment

CAP objectives (art. 39 TFEU): increasing productivity; ensuring a fair standard of living for the agricultural community; stabilizing markets; assuring the availability of supplies; ensuring that supplies reach consumers at reasonable prices

CAP objectives in the spotlight

- the range of the CAP objectives is broader than protecting competition (in particular, explicit socio-economic goal of ensuring a fair standard of living for the agricultural community)
- at the same time, the maintenance of effective competition on the market is needed to pursue some of the Art. 39 objectives (reasonable prices for consumers, increase in productivity)
- in order to attain the objectives set out in Art. 39, the TFEU provides the establishment of a common organisation of agricultural markets – which shall be limited to pursuing such objectives (Art. 40)
- the objectives set out in Art. 39 must be taken into account also by EU legislative bodies when establishing the extent to which competition rules apply to production and trade in agricultural products (Art. 43)

Effective CAP measures have to take into account the impact on all the Art. 39 objectives; in this perspective, the ECJ argues that «the maintenance of effective competition on the market» is one of the objectives of the CAP (C-137/00, *Milk Marque*, § 57 and 58)

Three questions

a. What can be achieved by means of the application of competition rules?

a.1 Merger control

- Merger control constrains the increase in market power at the different levels of the supply chain, when it is achieved by means of M&A and it results in a significant impediment to effective competition (horizontal, vertical, conglomerate mergers)
- It does not focus on bargaining power, but indirectly affects its evolution, by controlling the concentration process

a.2 Horizontal agreements

- Pursuant to Art. 101 TFEU, agreements between competitors are not prohibited as such, but only when they restrict competition and do not satisfy the Art. 101(3) requirements
- Competition policy therefore does not represent an obstacle to most horizontal cooperation agreements, especially between small competitors (e.g. farmers, small retailers)
- See in particular: de minimis notice; safe harbour established by block exemption regulations on R&D agreements and on production and specialization agreements (1217/2010; 1218/2010); Commission Guidelines on Horizontal cooperation agreements explaining how Art. 101 is applied outside the safe harbour for some categories of cooperation agreements including exchange of information, R&D agreements, production agreements, purchasing agreements, commercialization agreements
- The horizontal package is being revised: what about broadening the scope of BERs, e.g. including purchasing agreements?

a.2 Potential trade off with CAP objectives

- When horizontal agreements include restrictions by object/hardcore restrictions such as price fixing, output limitation and market partitioning, they are typically non compatible with Art. 101
- Moreover, the BERs and Guidelines on horizontal cooperation agreements refer to cumulative market share thresholds: no safe harbour for agreements involving all undertakings in a market

Potential trade off: if agreements which would be prohibited under standard application of Art. 101 are necessary for pursuing the CAP objectives, the establishment by EU legislators of a CAP exclusion to the application of competition rules (Art. 42 TFEU) may be justified

- However, the ECJ supports a narrow interpretation of exclusions/exemptions from the application of competition rules (inter alia, C-671/15, *Endives*)
- More generally, better regulation principles require that the boundaries of the exclusion meet the necessity and proportionality requirements =>caveat for future amendments to the CAP framework¹³

a.2 Cases

Competition authorities intervene, for instance, against:

- price fixing agreements between different producer organisations, not covered by the CAP exception (*Endives*)
- collective agreements limiting imports from other Member States (flour mills in France and Germany)
- buying alliances involving a large share of retailers

See

- ❖ ECN Report on competition law enforcement in the food sector, 2012
- ❖ Commission Staff Working Document SWD(2018) 450 final

a.3 Vertical agreements

- Vertical restrictions might be assessed also from a fairness point of view. However, the application of Art. 101 to agreements between undertakings operating at different levels of the value chain looks at their impact on competitive variables (price, quantity, quality, choice, innovation). The focus is not the bilateral relation, although in the past sectoral rules on motor vehicle distribution addressed also issues of bilateral power. With the modernization of EU competition rules (Reg. 1/2003), the application of Art. 101(1) and 101(3) becomes more ‘legally-oriented’, less discretion for the Commission in the application of Art. 101(3)
- Art. 101 does not impede impede vertical agreements unless they restrict competition
- Hardcore restrictions include resale price maintenance and (with some exceptions) territorial resale prohibitions
- De minimis, 2010 vertical block exemption regulation for distribution agreements + vertical guidelines

E.g. upfront access payments

An illustration of the competition law approach is provided by the section on upfront access payments to gain access to shelf space in agreements with large retailers (2010 Vertical Guidelines)

What are the concerns for competition?

- foreclosure of other distributors if the fixed fee leads to concentrate supplies in a limited number of distribution channels
- foreclosure of small suppliers

Potential efficiencies?

- risk sharing mechanism for the efficient use of shelves; decreasing the risk that suppliers launch suboptimal products at the expense of buyers

⇒ The theory of harm and the economic understanding of the impact on the market are the starting point for the application of Art. 101, paras. 1 and 3

a.4 Abuse of dominance

- Art. 102 can be used to avoid not only exclusionary abuses but also unfair exploitative conduct by dominant companies. May be useful to address issues of power in bilateral relations, but only when an undertaking is dominant

Summing up

In principle:

- scope for (narrowly circumscribed) CAP exclusion of the application of Art. 101
- ‘gap’ with reference to unfair unilateral practices by non dominant companies

b. Which boundaries for the regulation of fairness in B2B relationships?

Prior to the adoption of Directive 2019/633

- *recognition of widespread imbalances* in bargaining power in the food supply chain, which may lead to unfair trading practices. Smaller operators in the food supply chain, including farmers, may be especially vulnerable, although some market initiatives (agreements, consolidation etc.) may be taken to change the balance of bargaining power
- *voluntary initiatives*, supported by the Commission, have been undertaken (principles of good practice, Supply Chain Initiative since 2013) but some players do not adhere and need for strengthened enforcement
- *specific national rules* that protect suppliers against UTP in the food supply chain adopted in most Member States, either within competition law or outside it, but significantly divergent
- See Impact Assessment on the proposal for the UTP Directive, SWD(2018) 92 def. (e.g. abuse of economic dependence, prohibitions of below cost pricing etc.)

The path towards the UTP Directive

- proposal for a Directive ensuring a minimum Union standard of protection against practices that grossly deviate from good commercial conduct, are contrary to good faith and fair dealing and are unilaterally imposed (minimum harmonization)
- scope: sales of agricultural and food products, including processed products;
- turnover thresholds for suppliers v. buyers used to presume the existence of buyer bargaining power (no case by case assessment)
- the legal basis is Art. 43 TFEU; studies are undertaken to assess the impact of alleged UTP => pursuing the objectives of Art. 39 requires considering possible efficiency justifications of individual practices and avoiding rules which result in undesirable economic impact on the sector, in terms of productivity, competitiveness, innovation, quality and reasonable prices for consumers

e.g. JRC Technical Report on *Unfair Trading Practices in the Food Supply Chain*, 2017

The boundaries of the prohibition: black list

- A broadly worded prohibition of unfair B2B trading practices is discarded since it would entail high legal uncertainty => focus on specific practices, whose negative impact is rather uncontroversial
- Different formulation of the prohibition rule for different practices

Art. 3(1) – **Blacklist**: buyer practices always prohibited or *prohibited when specific conditions are met* (the exact formulation of the prohibition matters):

- late payments for perishable products;
- last minute order cancellations;
- unilateral or retroactive changes of contracts;
- payments not related to the sale of the product;
- forcing the supplier to pay for wasted product;
- refusal to confirm in writing the terms of the agreement;
- unlawful acquisition, use or disclosure of trade secrets;
- retaliation for the exercise of supplier's rights;
- compensation of the cost of examining customer complaints

The boundaries of the prohibition: grey list

- **Art. 3(2) – Greylist:** practices prohibited unless previously agreed in clear and unambiguous terms in the supply agreement or in a subsequent agreement between the supplier and the buyer:
 - a. the buyer returns unsold products to the supplier without paying
 - a. the supplier is charged payment for stocking, displaying or listing the products or making them available on the market
 - c. the supplier is required to bear the cost of discounts on products sold by the buyer as part of a promotion
 - d. and e. the supplier is required to pay for the advertising or marketing of the products by the buyer
 - f. the buyer charges the supplier for staff for fitting out premises used for the sale of the product

All these practices may have efficiency justifications

Comparison with the P2B Regulation

- In a different policy area, i.e. Digital Single Market Strategy, the P2B Regulation ((EU) Regulation 2019/1150) sets common rules aimed at promoting fairness and transparency in platform to business relationships (business users of online intermediation services and corporate website users of online search engines)
- Once again, in order to ensure that the EU rules are necessary and proportionate according to better regulation principles, not broadly worded rule, but specific obligations (transparency etc.)

Related issues

- The UTP Directive does not deal with fair pricing issues; sectoral rules, at the EU or national level, aimed at regulating pricing in bilateral relationships, such as prohibition to apply prices below average costs, may have unintended effects, especially if formulated as rigid general rules => need for further thinking?
- The implementation of the UTP Directive provides the opportunity to revise, from a better regulation perspective, all national rules on unfair trading practices in the food supply chain which go beyond the minimum standard set by the UTP Directive

c. Which model for enforcement?

Requirements for effective enforcement

- Pursuant to the UTP Directive, Member States:
 - shall designate enforcement authorities and points of contact for cooperation with other national authorities and the Commission
 - adopt rules on complaints and confidentiality adequate to deal with the ‘fear factor’
 - ensure that the authorities have the resources, expertise and powers to enforce their duties, including investigation and fining powers
- National choices relating to the enforcement system should take into account:
 - the broad scope of the UTP Directive (all levels of the food supply chain, including processed food and retailing) => need for neutrality of enforcers with respect to the involved interests
 - the existing national institutional framework for the application of national rules on UTP (e.g. Art. 62 in Italy) and its effectiveness
 - potential benefits of assigning the competence to competition authorities, which already apply complementary rules